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Indonesia's Fourth Five-Year  
Development Plan



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### **Ali Moertopo: In Memoriam**

A volume of 1.000 pages would not be enough to portray the man Ali Moertopo. As a “man of action” he has acted positively in 1.000 different problems of this country. While for many people intelligence and nobility of heart are different things, the man Ali Moertopo has succeeded in harmonizing and husbanding them in the service of his action and country. The harmony of intelligence and nobility of heart has been used in an excellent way to produce great ideas and concrete acts that were able to colour national life as well as the socio-political and socio-cultural dynamics in the Republic of Indonesia.

So complex were the problems he tackled and such a dominant role did he play in solving them though he has had no determining position, that with a never satiable administration one is tempted to find an answer to the puzzle: who is the man Ali Moertopo? This article does not pretend to answer it, but it just wants to add another to a series of existing predicates: He has been the vital elan of this Republic. A political concepthor who abounds in ideas and a capable operator.

Ali Moertopo, in addition to being known as a national important figure and great statesman, is also a founder and builder of the Centre for Strategic and International Studies (CSIS). In his function as its honorary chairman, he developed ideas, consulted and discussed without claiming personal infallibility. He upheld the line he has set as an attribute of the CSIS: an institution of study.

In his busy life, Ali Moertopo has been one of the few statesmen and state officials who did not feel busy and was not last in ceremonial functions and



short term routine work. While carrying out operational activities, his ideas kept flowing and racing toward the future: on national politics and international relations.

His intellectual instinct reached out to the future. His power of imagination is large. His thoughts are strategic. His actions are practical. With his intellectual prowess and sharp analytical power, Ali Moertopo has met the need of modern state concept. Unceasingly he has contributed his thoughts to the development of a developing society and has strengthened the life patterns of nation and country in accordance with the ideals established unanimously.

The goals of the life of society basically requires an ability to translate living ideals and ideas into realities of which the results can be enjoyed by the whole people. Ali Moertopo has attempted and succeeded in painting that translation process into the development of the New Order under General Soeharto. As one of the people who have determined the course of the history of the New Order he has been able to quickly deduce any goal into a set of actions.

Ali Moertopo is one of the main architects of the New Order who is very typical. With his intelligence he has developed ideas creatively in order to answer fundamental questions, that are able to affect the future of the New Order. He has firmly upheld the principle that the New Order is a Pancasila Order in a consistent and militant way under the guide of Pancasila. In a striking manner he has fought for the creation of the strategy of the New Order, mainly that of implementing Pancasila and the 1945 Constitution in a authentic and consistent way. At the beginning of the New Order, when people were still intoxicated with victory, Ali Moertopo already felt the need to re-arrange social institutions.

Ali Moertopo has played a role in the whole process of change and reform since 1966. The social reform he has been fighting for is based on Pancasila politics. The concept and process of his political reform had an element and colour of struggle, was geared to build political parties, was geared to programmes that were to take on the challenges of development. In this context, he pioneered the establishment of Sekber Golkar (Great Secretariat of the Functional Group) and later on encouraged Golkar to become a socio-political force of the New Order that does not discriminate because of race and religion. He also took part in re-arranging the political parties in order to regain a role in the life of the state.

As an important figure, Ali Moertopo has not discriminated against one's background. He has gathered exponents from all political spectrums and

social organizations, and has rejected provincialism. The basis and motivation of his relations was not confined to common conception. He has been able to mobilize various group for clear purposes. As an important national figure, he was very objective in the views of all circles.

His statesmanship is high as can be seen in his endeavours to form cadres without discriminating against one's group, tribe and religion. On many occasions, young cadres were encouraged to play a role. Many young people were interested and drawn to him. Whoever has managed to rise has become a pillar of political development of the future.

In the circles of the younger generation who were involved in business, Ali Moertopo encouraged them to play a role in development, by raising enthusiasm and professionalism. He had great interest in the youth and has often stressed the importance of regeneration. From the beginning of the New Order, he has always tried to persuade many young leaders to keep supporting the New Order.

His loyalty to his nation and country could not be doubted, it has been without flaws. As a tough, disinterested and spontaneous fighter, he defended the constitution and the case of the nation. His extraordinary ability was used exhaustively to help President Soeharto build this Republic. He has such a strong determination to serve the country and nation that he dared to take risks in his political behaviour. He was never absent in any phase of the nation's struggle, since the time he was a soldier until he became a senior officer, both during and after the physical revolution, in efforts to restore security, in the suppression of deviations from the 1945 Constitution and Pancasila.

The name of Ali Moertopo is so important in discussions on domestic as well as foreign politics. All political discussions seem impossible without mentioning Ali Moertopo. He has been most talked about since 1966. In the field of development he has contributed in formulating the 25 years acceleration of development. In foreign politics he has placed Indonesia in a broad geopolitical perception.

His political concepts are clear and he has been able to implement them in an organized way. As a fighter he had not only relied on power but also on intellect in his fight. With his thoughts he controlled his actions. His personality is strong and courageous. This courage has become another source of power to implement his conceptions. The struggle of which he was convinced would be carried out with courage and risks to himself, without compromise. He already acted when others were still thinking, so as to give the impression that he acted alone.



Now that the critical period of this nation has passed, Ali Moertopo goes. This has its own meaning. He leaves us as the moon leaves the night. He departs leaving beauty to meet again later. In truth, the earth finds itself between birth and death. What existed before his birth and happens after his death one does not know. Each of us has his own place assigned by his talents and good deeds. Whether one can face his Creator perfectly or not depends on whether or not his place is in accordance with the good deeds he has done.

*SOEDARSO*

## **Bush's Visit to Indonesia**

U.S. Vice President George Bush made an official visit to Indonesia from 10 to 12 May 1984. It was the second stop in his tour of Asia (Japan, Indonesia, India, Pakistan and Oman). The visit has given rise to speculations. It has been said, for instance, that his visit was some sort of compensation for the cancellation of President Reagan's visit of last November. It has also been reported that the main mission of Mr. Bush's visit was to convey President Reagan's message to President Soeharto and to brief the latter on the outcome of the former's visit to China (26 April - 1 May).

Although not fully, Bush's visit was indeed intended to compensate for Reagan's cancelled visit to Indonesia. This is in accordance with the policy so far adopted by the U.S. to establish closer relationships with countries in Asia and the Pacific. Within this framework, President Reagan visited diverse countries (Japan, South Korea and China) and had planned to visit the Philippines, Indonesia and Thailand but cancelled it on account of the assassination of the Philippines' opposition leader, Benigno Aquino in August 1983. In addition he sent his assistants.

That Indonesia is chosen to be visited is not surprising. The U.S. is aware that Indonesia is not only the biggest country in Southeast Asia but has also a significant role to play in international forums such as the U.N., Non-Aligned, the Islamic Conference, OPEC and ASEAN. Hence Washington deems it necessary to give a positive response to the dynamism and initiatives of Indonesia's foreign policy. This was indicated by Bush's statement in Jakarta that the U.S. highly appreciates Indonesia's independent foreign policy and



acknowledges that to date Indonesia has played a significant role not only in the Southeast Asian region but also in that of the Pacific.

The main purpose of George Bush's visit was to convey President Reagan's message to President Soeharto and to brief the latter on the outcome of the former's visit to China. This is an indication that the U.S. is sensitive to the feelings, aspirations and interests of the ASEAN member countries particularly Indonesia. Since a long time the growing relationship between China and the U.S. has worried Indonesia because it may be detrimental to the ASEAN's (Indonesia's) interests. The U.S. support to China may decrease the country's aid to Indonesia. Aside from that, since China and the ASEAN have the same interests in the U.S. market, the growing Sino-U.S. relationship will increasingly heighten export competition especially that of oil and other resources. The military aid promised by the U.S. to China may also step up China's capability to support the Southeast Asian communist groups. In this regard Mr. Bush gave the assurance to Indonesia that the Sino-U.S. relationship will not harm and endanger the interests of the ASEAN member countries, especially Indonesia.

Hence George Bush's visit may be interpreted as an U.S. attempt to foster mutual understanding and to prevent misunderstanding. To date the U.S. seems to have given priority to its relationship with those countries with which it confronts the Soviet Union and its allies. For a country with an independent foreign policy such as Indonesia, the U.S. foreign policy is rather annoying. Until now Indonesia has refused to involve herself or be involved in the Soviet-U.S. conflict. Indonesia feels that the U.S. foreign policy to mobilize as much as possible support to confront the Soviet Union may endanger the security in the Southeast Asian region. During his visit Mr. Bush showed his understanding for Indonesia's concern and did not touch upon the Soviet threat. It is expected that due to the U.S. understanding, the relationship between Indonesia and the United States will always be smooth.

*Endi RUKMO*

## **IGGI Loans: National Pride Calling for Caution**

Amidst difficulties faced by many countries in managing their debt service Indonesia has obtained facility for a new loan. At least this was reflected in a recent IGGI meeting. And, indeed, it was hardly a week since Brazil's an-

nouncement of rescheduling its debts when the IGGI made a new commitment to Indonesia of US\$2,462.5 million in aid. This consists of US\$698.5 million from IGGI countries and US\$1,764.0 million from international agencies like IMF, World Bank, ADB, EEC, UNDP and UNICEF.

This is evidence of the trust donor countries have in Indonesia's economic policy. If last year the IGGI lauded it, this year they have again given it their support. According to Prof. Widjojo Nitisastro, this is something which evokes national pride. However, the latest development in the monetary field calls for caution.

While foreign debts are intended to complement government savings for the financing of development, the composition ratio of government savings to foreign debts changes annually in accordance with an uncertain pattern. In the 1984/1985 draft of the state budget the share of foreign aid is estimated at Rp4,413.82 billion or 42.2 per cent of the development budget of Rp10,459.3 billion.

Whether the amount of aid agreed upon by the IGGI will, in effect, be drawn only partly or even less depends upon the development of the balance of long-term capital, including that of non-governmental current accounts abroad.

It is noted from several sources that debts drawn by Indonesia are rising year by year. By 1982 debts so drawn totalled US\$18,421.2 million. But while some of the debts will have meanwhile reached maturity and will therefore require repayment of both capital and interest, the maturity of debts, on the average, tends to become shorter concurrently with an increasingly shorter grace period. If in 1973 the average maturity period was 23.7 years, in 1982 it became 15.1 years. This also applies to the grace period, which was 6.2 years in 1973 and 4.9 years in 1982. This trend is characteristic of the debt service in the years to come.

It has to be admitted that Indonesia's achievement in debt repayment has not been disappointing so far. Unlike other countries which have to reschedule their debts, Indonesia is not in that group of debtors who worry their creditors. But this does not mean that the same problem will not be faced by Indonesia in the foreseeable future. Indonesia's ability to repay debts incurred in previous years was sustained, among other things, by the debt profile itself. With the still relatively long maturity and grace periods the burden of repayment will certainly not be as heavy as that in the years to come.

Although constant in volume, the new loans made subsequently will relatively drop in significance with the rise in the repayment burden. It is this trend that will probably be faced in the future.



The above statement is supported by the ever-increasing interest rate of the country's debts. If in 1972 the average interest rate was 5.9 per cent, in 1982 it went up to 9.4 per cent. This increase occurred concurrently with the increase in the installment payments which means an increase also in the total repayment amount. This can be seen from the government's debt service which in 1973 was only US\$92.7 million but which in 1982 rose to US\$852.1 million. Finally, the ratio of nett transfer of source, that is, new loan less debt service in a certain year divided by new loan, declined from 81 per cent in 1973 to 40 per cent in 1982.

The development of the international capital market also plays a significant role in determining the country's debts. The tendency has hitherto shown that the rise in the interest burden of the government's debts is closely linked to the rise in the U.S. prime rate or LIBOR (London). This linkage with the commercial interest rate is also noticeable in many other countries, including Brazil. The rise of 1 per cent in the U.S. prime rate has, for example, brought about an increase of US\$500 million in Brazil's debt burden. If the prime rate goes up again in the future, as is feared at present, Indonesia's burden of debt repayment will also go up. The increase of LIBOR by 1 per cent, for instance, is expected to cause an increase in the current account deficit by US\$90 million. Some projections reveal that Indonesia's debt service will have reached US\$3,508.8 million in 1987 and US\$2,791.0 million in 1990. And this will apparently continue to rise.

The government's facility in managing its debts so far has also been sustained by the stable commitments of the donor countries. But whether this tendency will continue in the years to come remains to be seen.

The present adverse world economic condition has, *inter alia*, brought about a rise in the need for foreign aid in the developing countries. Conversely, however, this adverse condition has also led the developed countries not only to reduce their fund supplies but to tighten them up in view of the unsatisfactory management of the debt service by most of the developing nations. We should therefore be well aware of this tendency, because the facility of obtaining loans enjoyed so far is inclined to become less and less available in times to come.

Provided new loans are still easily obtainable, the price asked for is likely to go up. The severe competition inherent in obtaining much-needed but scarce funds indicates that the bargaining position of the debtors has become increasingly weaker. In other words, the room for activity in debt management tends to become smaller. This also indicates that the influence of donor countries on the selection of development projects has become stronger, a condition that is not exactly desirable. But nevertheless we want to hold on to the development ideals that reflect our national aspirations.



This fear is partly due to lack of information on the part of society regarding the pre-requisites required by donor countries insofar as it concerns the granting of loans, especially the criterion for the selection of projects that will prove beneficial to all parties concerned. However, to what extent these national aspirations are sacrificed remains to be seen.

But an encouraging point insofar as it concerns the function of foreign debts is the declining tendency of the percentage of foreign aid needed to finance development. If in Pelita I this was 75 per cent, in Pelita II it went down to 56 per cent and in Pelita III to 36 per cent. This trend may be used to enhance our bargaining position, but nominally the need for loans tends to increase, because in the next few years at least they are still urgently required. So the above estimates are still quite relevant.

If the function of foreign debts is, *inter alia*, directed towards closing the foreign exchange gap, then solution of the problem of debt service depends upon our export capability. But are our exports capable of answering the questions that arise from these foreign debts? A projection with a rather apprehensive tone would apparently be necessary if we could not only avoid having current account deficits but turn them into surpluses as well.

Many attempts have been made to promote non-oil exports. These include, among other things, the introduction of general and special export policies for each export commodity, the evaluation and further adjustment of which is deemed necessary with a view to greatly improving the end results.

Apart from oil products and petrochemicals, often mentioned today as potential non-oil export commodities are processed wood products, rattan, textiles and ready-made clothing, fishery products (particularly shrimps), and agricultural products with palm oil topping the list.

The export of processed wood products has developed particularly well since the promulgation in 1980 of the joint decree of the three ministers concerned and will be further promoted, both in terms of quality and quantity. We should, however, be aware of the fact that in the years to come export of these products might have to face a not insignificant challenge. Some information reveals that Japan as a potential importer of wood products is now developing its own forests which are expected to bring forth yields in 10 to 15 years from now. Hence we should endeavour to expand the market and at the same time resort to diversification of the products. For instance, particle boards and cement boards are quite potential, not only export-wise but also domestically.

Despite many challenges, textiles and ready-made clothing will still constitute important commodities in the future. A policy should be adopted

that would further promote the export of these products. According to exporters, the incentive that takes the form of export certificates is no longer effective, because it is essentially a disguised subsidy since export of these commodities is already quite lucrative. It has even been hinted that it has encouraged irregularities among certain officials.

The export of fishery products appears to be quite promising too, especially that of shrimps, frog legs and tuna. It also seems very likely that an intensification of shrimp ponds to an extent of 120,000 hectares and an extension of up to 100,000 hectares will be further intensified in the future. These efforts will not only be conducive to increasing export of fishery products but be a means of improving the living standard of fishermen.

The production of petrochemicals also shows an encouraging trend. Besides being a positive factor of increasing export of this product, the industry also serves as a means of providing employment and acts as an agent for import substitution.

Apart from the above commodities, there are certainly many other export products that can be developed. Thus through export development the country's debt service can be managed in stages without much difficulty and, besides, it will not hamper development in general.

It seems obvious that our debt service capability depends to a large extent upon our ability to manage funds so obtained in the best possible manner. This includes, among other things, the selection of projects to be tackled and the supervision of the implementation thereof. The most profitable projects in terms of labour absorption capacity and ability to increase export should certainly be given top priority status.

Besides, efforts to step up economic efficiency should not be taken lightly, because the high cost economy might hamper export development. Thus improvements directly or indirectly affecting production cost should be made. The policy of revoking licences is worthy of note here. In April of this year, for example, 17 kinds of business licences from the Department of Trade and 16 from the Department of Forestry were revoked. This is a good beginning for the further adoption of policy on licences which may directly or indirectly stimulate export which in turn may eventually determine whether, and to what extent, Indonesia is capable of managing its debt service on schedule.

*Sudarsono HARDJOSOEKARTO*



## The Introduction of Compulsory Education

On May 2, 1984, President Soeharto announced the introduction of compulsory education throughout the whole territory of Indonesia. The announcement was officially made with a ceremony at Gelora Senayan in Jakarta that was attended by 110 thousand people. That occasion marked the beginning of the implementation of the national program of compulsory education. The main reason prompting the government to take the step is the desire of the Indonesian people to advance and pursue one of the goals established in the Preamble of the 1945 Constitution, namely to improve the intellectual level of the nation.

The purpose of implementing compulsory education on a national scale is to enable parents, pursuant to their rights and obligation, to send their children aged 7-12 years to the elementary school until they graduate, while the government has to provide all the educational means and facilities needed in the process of the implementation of compulsory education. However, due to the still limited capability of the government to deal with the matter, parents and the community are expected to contribute in providing the means and facilities in accordance with the conditions of each area. Remoted areas, for example, generally lack elementary school teachers and accordingly parents or other members of the community who have finished their elementary school education may assist teachers by becoming tutors, or give other forms of aid. This way, compulsory education will become the common responsibility of the government, parents and the community who are to provide educational means/facilities and teachers so as to enable school-age citizens to exercise their rights on education in accordance with the provision of Article 31, Paragraph 1 of the 1945 Constitution.

The 1980 population census reveals that out of 24,692,291 (7-12 years old) children, 2,647,040 children never enjoyed schooling and 1,116,041 are drop-outs throughout Indonesia (see: *The 1980 Population Census by Province, serial L No. 3, Central Bureau of Statistics*). And in view of Indonesia's annual population growth of 2.34 per cent the number of school-age children will also increase. This means that the 7-12 years old children who have never come to school will also increase in number.

That those children (7-12 years) are not yet/not able to enter elementary school is due to the following factors: (1) their domicile in remote areas; (2) the family's economic condition; (3) local tradition; and (4) the lack of educational means/facilities.

Generally the remote areas are not yet within each of the network of transportation and communication so that the government faces difficulties in



building schools. Hence the 7-12 years old children of this population group have not as yet been able to enter school. In the process of making this compulsory education program successful the government has built small elementary schools in those remote areas. By that are meant schools with only one or at the most three classrooms and with only one or two teachers. The government have also built houses for the teachers.

The economic condition of the family denotes the living condition of the family whose total income is smaller than or equal to the total expenditure in one month to meet its basic needs, namely food, clothes and housing. To pay for other needs such as sending the children to school is beyond their means. This group of people considers school as a formal educational institution which is beyond their financial means, although they want to send their children to school. The children of this environment generally help their parents in their work such as working in the field, catching fish, selling newspapers, shining shoes, working as conductors of mikrolets (minibuses) and collecting used goods. For the children of this category the government has developed "pamong" elementary schools and a "working while you study" scheme of Package A. In the Pamong Elementary School (managed jointly by the parents, society and government) all expenses including those for books are paid by the government. The children only come to school to be taught and trained in various skills in accordance with their interest. This way the societal tradition for not sending their children especially the girls to school may likely be overcome. The provision of elementary school buildings through the Presidential Instruction projects since 1973 greatly supports implementation of this compulsory education.

Children aged 7-12 years who are not physically disabled, coming from families with sufficient economic background, and who do not live in remote areas have to enter conventional elementary schools or madrasah ibtidaiyah (Islamic School). For physically disabled children the government provides Special Schools (type A, B, C, D, and E).

It is obvious from the above explanation that the government has made the necessary preparation to make the implementation of compulsory education successful. Since the school year of 1979 the Directorate General of Elementary Education of the Department of Education and Culture has even made preparations by opening Projects for the Improvement of Compulsory Education (PPWB), among others at Seyegen, the District of Sleman, Central Java. From experience in those projects the government knows the difficulties to be faced in the implementation of compulsory education, i.e. the attitude of parents who still want their children to help them in their daily chores and the attitude of children in class who become easily offended if they are rebuked by their teachers and who sometimes challenge their teachers to fight.

Efforts to settle such difficulties may be made through close cooperation between teachers, the village/kelurahan apparatus, youth organization or Family Welfare Promotion (PKK) in jointly giving information to parents on the importance for their children to participate in compulsory education. In addition, field officials, in this case the teachers, should adopt a mature and wise attitude. Through all available mass media the government should give information on this compulsory education. Furthermore, what needs to be taken into consideration is the re-arrangement of the Elementary School curriculum so as to enable school-age children, who are not able to continue their study in secondary schools, to acquire skills for employment.

*BABARI*

# Indonesia's Fourth Five-Year Development Plan

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## Introduction

On April 1, 1984, Indonesia entered its Pelita IV (Fourth Five-Year Development Plan) that is a crucial period in its national development. In this Pelita the basic framework will be laid for the Indonesian nation to grow and develop further. This framework will be consolidated in Pelita V so as to enable Indonesia to take-off in Pelita VI with a view to accelerating development toward the establishment of a just and prosperous society based on Pancasila as stated in the GBHN (Broad Outlines of the State Policy) of 1983-1988.

As in the preceding Pelitas, in Pelita IV economic development has been established as the priority with the aim of improving the living standard and the welfare of the people. In addition to deciding steps to achieve those goals, the government has targeted an average economic growth of 5 per cent per year. To attain this target, an average investment of 26.7 per cent of the GNP per year will be needed. The financing of that investment will mainly rely on domestic savings, while foreign resources will be complementary. Domestic investment is expected to derive 21.6 per cent from the GNP and 5.1 per cent from foreign aid.

With regard to the financing of investment from domestic savings, the government expects 8.9 per cent of the GNP to be drawn from the public sector saving and 12.7 per cent from that of the private sector. For that reason the government makes endeavours to raise its saving, among others by improving the taxation system and tax collection, and to raise private saving by mobilizing funds of the people through financial institutions, including banks, in the form of deposits, emission of certificates and other forms of saving. Thus the private sector is expected to play an important role in development activities.

The government is also to continue to promote export activities, particularly non-oil and non-gas export. This non-oil and non-gas export is expected



to grow 17 per cent per year, while the increase of the export of oil and gas will be only 5.8 per cent per year. In the years ahead, the growth rate of oil export will not be as high as in the past, due to growing competition and successful oil conservation efforts in industrialized countries. For that reason, the government encourages the export of goods and services outside oil and gas by improving the production efficiency, the quality of goods, transportation, and taxation facilities and by providing credit facilities under adequate terms and so on.

Various steps have been designed by the government to accelerate the economic development. But to be successful those steps need to be supported by an understanding of the economic problems that are expected to arise in Pelita IV. Past experience shows that development endeavours have not always achieved optimal results due to the lack of the ability to anticipate, slowness to act and to react and tardiness in taking initiatives. Those problems are likely related to foreign trade, the balance of payments problem, dependence on other countries, employment, taxation and the role of the private sector. If economic development is to achieve its objectives, the government should deal seriously with those problems.

Although development in the economic field is given priority, it does not follow that development in other fields is neglected. In the book of Repelita IV it is stated that parallel with the priority of the economic development, development in the political, socio-cultural, defence and security fields will be increased so as to support the progress achieved by economic development. Moreover, there is an increasing awareness that development in the economic field is not just economic in nature, but also constitutes a means for achieving the ultimate goal of national development, that is to enable people to attain a better and fuller life. Therefore, development is socio-cultural in nature. In addition, political development has also an important role to play because it constitutes a part of national development that is basically geared to strengthen national consciousness in accordance with Pancasila and the 1945 Constitution. Development outside the economic field is to be carried out in conjunction with the progress made in the economic field. On the other hand, the increase of results in the economic field will in turn provide wider resources for development in the other fields.

Indonesia's Pelita IV is the general topic of this special issue. The country's overall development over the next five years will be discussed in its different aspects in 7 articles. It is common knowledge that since the rise of the New Order, national development has been Indonesia's foremost concern.

# Indonesia's Pelita IV: 1984/1985 - 1988/1989

Anwar NASUTION

## INTRODUCTION

The prospect of economic growth in Indonesia during the current Fourth Five-Year Development Plan (Pelita IV) critically depends upon external developments and adequate domestic economic management, including sufficient adjustment to external events. In addition, efforts to step up the mobilization of domestic saving through taxation and the banking system are also crucial. As regards adverse exogenous shocks, Indonesia is affected by the successful energy conservation and oil substitution programs in oil consuming countries, the prolonged recession in early 1980s, and the rise in real rates of interest.

The weakening of world demand for oil and oil glut have led to OPEC's decisions to cut back both the price of oil as well as its production, beginning since early 1983. The severe prolonged recession in industrial countries has induced an overall decline in nominal prices of non-oil primary export commodities. Real prices of such goods were at their lowest level for thirty years in 1982.

The sharp increase in nominal interest rates in the international market from 1979 was subsequently sustained at a time when world inflation was declining. This resulted in very high real rates of interest. The increase in interest rates is originated from restrictive monetary policies in the United of

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Paper presented at the *Fourth Indonesia-Korea Conference*, held in Seoul, Republic of Korea, on May 21-23, 1984, sponsored by IFES, Kyungnam University (Seoul) and CSIS (Jakarta). Dr. Anwar Nasution is Lecturer in Monetary Economics at the Faculty of Economics, University of Indonesia.



America. The shocks wave from the very high American interest rates was one of the most disturbing factors for the world economies. It did not only increase the burden that borrowers had to pay on their external debt but also it created dilemmas for other nations in managing their domestic economies. If the rest of the world were to follow the higher American interest rates, the consequences for domestic industries, public debt and employment will be detrimental. Not to follow would imply an accelerated depreciation of domestic currencies. In the medium run, devaluation would also increase the costs of dollar-prices imports which would in turn significantly fuel domestic inflation. The interest rates war between nations has caused uncertainty in foreign exchange rates. High domestic unemployment rates have increased pressures for protectionism which have resulted in reductions of international trade.

The effect of the shocks on Indonesia's growth has been dramatic. Indonesia's real GNP expanded by only 2.3 per cent in 1982 and by 3 per cent in 1983 compared with 7-8 per cent during the previous decade and 10 per cent in 1980. This means that for the first time, during the period of the present government, per capita income of Indonesia remained stagnant in 1982 and 1983.

To restore external viability, the government has taken prompt and drastic macro economic measures in order to curb excess demand and balance of payments pressures. For the second consecutive year, an austerity budget was introduced in January 1984. To make up for the decline in export earnings, the government increases its foreign borrowing, promotes exports of non oil commodities including tourism, restricts imports of luxury goods, discourages foreign travel and steps up the use of domestic production. On March 30, 1983 the rupiah was devalued by 28 per cent. At the same time, monetary policy was tightened to reduce domestic demand and to reverse pre-devaluation capital outflow. On June 1, the government abolished ceiling cum selective credit policies at state owned banks, at least for non priority sectors. Since then the state owned banks have been free to set their deposit and loan rates for non-priority sectors. In May, the government announced that nearly 50 capital and import intensive public sector projects, jointly worth more than US\$20 billion, were to be shelved or rephased or made available to other sources of financing. In addition, the government has also taken several steps to invite larger participation of the private sector in economic activities as well as some measures to liberalize, deregulate and decontrol the economy.

Under such a difficult world economic environment, Indonesia enters Pelita IV. The objectives of the present Pelita are similar to previous ones, namely, to achieve economic growth and equity and to preserve stability. The average target during Pelita IV is 5 per cent per annum, which is quite modest compared to the present rate of population growth of 2.3 per cent per annum.



In order to attain a higher income per capita, the government intends to intensify its population control program with the goal of reducing population growth to 2 per cent.

The organization of this paper is as follows. An analysis of past, present, and projected future growth during Pelita IV is presented in the next section. A review of the Indonesian balance of payments follows thereafter. In the fourth section an analysis is presented on the recent government budget and fiscal policies, which is then followed by a review of monetary policies in the fifth section. Lastly, the sixth section contains a concluding remark.

## GROWTH PROSPECT AND STRUCTURAL CHANGE

As indicated in the preceding section, as a consequence of world wide recession and the accompanying sharp decline in the price and volume of oil exports, Indonesia's resource availability has worsened since the last two years. This has led not only to increased pressures on the balance of payments but also to reduced government revenues to a downturn in domestic income and to slackened investment outlays. Since the first oil shock in 1973, Indonesia's economy has been too dependent on oil. About two thirds of government revenues and eighty per cent of the country's export value have been derived from oil. For every dollar fall in the price of oil, Indonesia loses about US\$330 million of export revenues.

Because of the resource constraints, a reduction in growth rates from the one prevailing in the previous Pelitas is inevitable in the present Pelita IV. However, in order to provide adequate employment for labour force which is growing at 2.6 per cent per year, it is of great importance to restore growth in the non-oil sectors to about 6 per cent per year. At a growth rate substantially lower than that level, Indonesia will have difficulty in creating sufficient employment for the 15 to 20 million new entrants to the labour force.

Except for mining and quarrying, the targeted sectoral rates of growth in Pelita IV are consistently lower than their actual annual rates in 1973-1980 (Table 1). The targeted sectoral annual rates of growth for Pelita IV are as follows: agricultural, 3 per cent; mining and quarrying, 2.4 per cent; manufacturing, 9.5 per cent; construction, 5 per cent; transportation and communication, 5.2 per cent, and the remaining sectors: 5 per cent. With these rates of growth the GDP composition is expected to shift from the agriculture sector to mining and quarrying and manufacturing. Table 1 also reveals that the rates of growth of GDP and of its components is positively related to the development in oil price. In other words, oil has been an engine of growth in the Indonesian economy.

Table 1

INDONESIA: GROSS DOMESTIC PRODUCT BY INDUSTRIAL ORIGIN AND  
EXPENDITURE CATEGORIES AT CONSTANT 1973 MARKET PRICES: 1968-1982  
AND PROJECTION FOR PELITA IV, 1984/85 - 1988/89 (Rp billion)

	1968	1973	1978	1982	Average Annual Growth Rate (%)					GDP Composition (Est.)	
					1968-73	1973-78	1978-82	1982-89	Pelita IV	1983/84 (%)	1988/89 (%)
<b>A. GDP by Industrial Origin</b>											
1. Agriculture	2,203.4	2,710.0	3,134.8	-3,669.8	4.23	2.96	4.02	3.71	3.43	29.3	26.4
2. Mining & quarrying	37.0	831.0	1,048.8	939.8	17.46	4.77	-2.71	6.85	1.38	7.4	6.6
3. Manufacturing	349.1	650.0	1,235.6	1,900.7	13.24	13.71	11.37	12.87	12.66	15.8	19.4
4. Construction	87.1	262.0	528.9	757.8	24.64	15.08	9.41	16.71	12.52	6.3	6.3
5. Transportation and communication	152.1	257.0	514.2	716.6	11.06	14.88	8.65	11.71	12.07	6.0	6.0
6. Other	1,316.3	2,043.4	3,104.2	4,340.7	9.19	8.92	8.74	8.90	8.73	35.3	35.3
Gross Domestic Product	4,479.7	6,753.4	9,566.5	12,325.1	8.56	7.21	6.54	7.5	6.91	100	100
<b>B. GDP by Expenditure Categories</b>											
1. Total consumption	3,959.8	5,506.7	8,107.7	12,473.6	6.82	8.04	11.37	8.54	9.51		
Private consumption	3,560.6	4,790.7	6,879.5	10,697.5	6.11	7.51	11.67	8.17	9.34		
Government consumption	399.2	716.0	1,238.2	1,776.1	12.39	11.40	9.66	11.25	10.62		
2. Gross Domestic Investment	418.3	1,208.0	2,332.9	3,636.7	23.63	14.07	11.74	16.70	13.03		
3. Export	595.8	1,354.3	1,824.3	1,444.3	17.85	6.14	-5.67	6.53	0.72		
4. Import	494.2	1,315.6	2,698.4	5,229.2	21.63	15.45	17.99	18.35	16.57		
C. Nominal Price of Crude Oil (\$/barrel)	—	3.73 <sup>1</sup>	13.55 <sup>2</sup>	35 <sup>3</sup>							

Sources: 1. Central Bureau of Statistics, *National Income Accounts*, various issues.

2. Repelita IV, 1984/85 - 1988/89, volume 1.

Notes: <sup>1</sup>Effective since April 1973.

<sup>2</sup>Effective since January 1977.

<sup>3</sup>Effective since January 1981

## **Agricultural and Mining**

The agriculture sector in Indonesia absorbs more than 60 per cent of the total labour force and contributes about a quarter of the GDP. Because of these reasons Pelita IV attaches high priority to the agriculture sector. The food crops sector accounts for 60 per cent of the total agricultural output and the rest comes from estate crops, livestock and fisheries.

To release foreign exchange from the increasing import of food, production of rice is targeted to increase by 22 per cent in Pelita IV. To achieve this objective through transmigration programs the government plans to open new rice fields outside Java, to expand and improve the existing irrigation system and to continue the existing extension service program with subsidized credits which is known as Bimas. With intensification through the Bimas program, the average productivity of rice fields is expected to increase by 13 per cent during Pelita IV. The production of rice and other food crops in Indonesia is entirely in the hands of individual small farmers, and output is dependent on their choice. To increase production, therefore, it is also important to ensure that adequate supplies of required inputs are available for purchase by farmers when needed, within an incentive framework which will support their use.

About 90 per cent of value added produced in mining and quarrying is derived from oil and gas. Prospect for international oil market is uncertain during Pelita IV due to the hesitant economic recovery in OECD countries. Unlike oil, however, natural gas is not so much affected by the present economic recession. The large capital cost of LNG production and transportation requires that production be tied to long-term contracts. Nevertheless, the LNG price is indexed to that of crude oil.

## **Manufacturing**

The development of a modern industrial base in Indonesia has only recently begun. During most of the period from 1930 up to the late 1960s, the Indonesian economy had been largely cut off from foreign influences. Immediately after it came to power in 1966, the new Soeharto government introduced economic stabilization, rehabilitation, and new development programs that were more conducive to growth in the industrial sector than previous policies had been. Even after a decade of rapid expansion during the 1970s, however, the Indonesian manufacturing sector is still relatively small and underdeveloped.

The dualistic structure of the Indonesian manufacturing sector can be shown by the dominance of a small number of modern enterprises in terms of



output, value added and wages (Table 2). As indicated in the table, in 1974 the modern sector (large and medium scale establishments) comprising less than 1 per cent of manufacturing firms accounted for 79.9 per cent of value added and output but only for 13.5 per cent of employment. On the other hand, the smaller scale traditional sector (cottage and small industries) consisting of over a million enterprises, contributed about 22.1 per cent of output and employed 86.5 per cent of manufacturing workers. Average labour productivity, defined as value added per worker, in the modern sector of industry was almost 40 times higher than in the traditional sector.

Table 2

## STRUCTURE OF THE MANUFACTURING SECTOR BY SCALE OF OPERATION, 1974

	Total Absolute Level	% of Manufacturing Sector			
		Cottage Industry	Small Scale Industry	Medium Industry	Large Industry
No. of establishments	1,289,800	95.7	3.7	0.5	0.1
- Using power	4,649	nil	7.3	68.5	24.1
No. of person engaged:	4,904,800	79.5	7.0	4.2	9.3
- Unpaid	3,802,800	97.8	2.0	0.2	
- Paid	1,102,000	16.1	24.4	18.2	41.3
Gross output (Rp. bln.).	1,653	12.2	9.5	12.3	66.0
Value added (Rp. bln.).	613	13.5	8.6	15.9	62.0
Wages and salaries (Rp. bln.).	120	8.4	13.6	15.9	62.1

Sources: BPS, *Statistik Industri*, various issues; and *Industrial Census 1974/1975*.

While the modern sector has been using imported modern machinery and technology, the traditional industries continue to use traditional methods of production relying principally on manual labour rather than electric power. The modern industrial sector consumes more than 90 per cent of total industrial electric use to produce goods that are often similar to, but of better quality and often cheaper than those of traditional industries. More than 40 per cent of the value added in the modern sector is in food, beverages and tobacco, about 18 per cent in chemicals, and 12 per cent in textiles. As a result, the modern sector is displacing the traditional sector in producing many products. However, the second half of the 1970s witnessed product diversification in the modern industrial sector in the area of basic metal and non-metal products as well as in fabricated metals.

By international standards, growth in the manufacturing sector in Indonesia during the 1970s has progressed remarkably well. During the first half of the decade, 1971-1976, real industrial output, recorded in constant prices, grew by 13.7 per cent per year and continued to grow at a lower, but nevertheless quite rapid, annual rate of 11.6 per cent between 1976 and 1978. During the whole decade, 1970-1980, the annual growth rate was 12.8 per cent, which is higher than that of the overall GDP or its other sectoral components during the same time period.

A number of factors have contributed to the slowdown in the manufacturing sector since 1975. First, there were the difficulties caused by the problems of the state oil company, Pertamina, during 1974. Due to its sizable role in the economy, abrupt cessation of many of Pertamina's domestic activities created problems for domestic enterprises whose lines of business were directly or indirectly related to the activities of the state owned oil company. Second, there was the more basic problem of competition from imports as a result of the "Dutch disease" (upward pressure on exchange rates), which, in turn, resulted from the strength in the balance of payments caused by the "oil boom." On November 15, 1978, this was corrected by the government by devaluing the rupiah by more than 50 per cent against the U.S. dollar. Third, the "easy" phase of import substitution for some industries such as textiles, electronics and motor vehicles, may have come to an end.

During the course of Pelita IV, the government plans to establish a closer linkage between the modern segment of the manufacturing industry with the traditional one. In the modern sector, the government will continue to develop resource based industries, shipyards, heavy industries, electronics industries, and the airplane assembly plant.

As of now, exports account for less than 4 per cent of the domestic output of the manufacturing sector. This share is projected to rise in Pelita IV. Whether the government can attain this objective depends upon domestic policies to promote those exports, the pace of economic recovery in OECD countries as well as on the state of international protectionism.

## BALANCE OF PAYMENTS

Indonesia's balance of payments reached its peak in 1981/1982 after the second oil shock in 1979 (Table 3). The oil glut and world wide economic recession started to affect Indonesia's economy in 1982. Her net export value dropped by 38 per cent in that year and non-oil export by 30 per cent. On the other hand, non-oil import continued to rise, though less rapidly than in preceding years. As a result, a current account surplus of US\$2 billion in

Table 3

## BALANCE OF PAYMENTS, 1978/79 - 1988/89 (US\$ million)

	1978/79	1979/80	1980/81	1981/82	1982/83	1983/84 est.	Repelita IV Projection				
							1984/85	1985/86	1986/87	1987/88	1988/89
<i>Exports (f.o.b.)</i>	11,353	18,511	22,885	22,994	18,638	19,310	19,875	22,433	25,332	28,223	31,116
Oil	6,858	10,995	15,187	16,482	12,283	11,861	10,644	11,873	13,463	14,664	15,766
LNG	516	1,345	2,111	2,342	2,461	2,279	3,181	3,551	3,854	4,344	4,597
Non-oil	3,979	6,171	5,587	4,170	3,894	5,170	6,050	7,009	8,015	9,215	10,753
<i>Imports (f.o.b.)</i>	-8,443	-10,722	-14,242	-17,911	-18,496	-17,103	-17,287	-18,979	-20,844	-22,906	-24,799
Oil	-1,664	-2,586	-3,557	-4,799	-4,223	-4,114	-3,885	-4,260	-4,573	-4,979	-5,304
LNG	-47	-86	-124	-117	-142	-185	-212	-237	-260	-291	-301
Non-oil	-6,732	-8,050	-10,561	-12,995	-14,131	-12,804	-13,190	-14,482	-16,011	-17,636	-19,194
<i>Services (net)</i>	-4,065	-5,591	-6,512	-7,873	-7,215	-6,918	-7,257	-8,026	-8,578	-9,087	-9,548
<i>Balance on Current A/C</i>	-1,155	+2,198	+2,131	-2,790	-7,073	-4,711	-4,669	-4,572	-4,082	-3,770	-3,231
<i>Government borrowing</i>	2,208	2,690	2,684	3,521	5,011	6,030	5,481	5,079	5,070	5,568	5,713
Program aid	94	239	118	50	21	101	67	42	44	48	51
Project aid	1,943	2,311	2,420	2,614	3,400	3,905	3,248	4,037	4,352	4,920	5,278
Other	171	140	146	857	1,590	2,024	2,166	1,000	674	600	384
<i>Public debt repayments</i> (principal only)	-632	-692	-615	-809	-926	-988	-1,297	-1,380	-1,665	-2,169	-2,536
<i>Other capital</i>	392	-1,315	-361	1,140	1,795	1,244	695	1,097	927	821	692
<i>SDR</i>	64	65	62	—	—	—	—	—	—	—	—
<i>Monetary investments</i>	-708	-1,690	-2,736	988	3,280	-2,061	-200	-224	-250	-450	-638
<i>Errors and omissions</i>	-169	-1,256	-1,165	-2,050	-2,087	487	—	—	—	—	—

Sources: 1. Government Budget (Nota Keuangan dan RAPBN) 1984/1985

2. Repelita IV, volume 1.



1980/1981 turned into a deficit of US\$2.8 billion in 1981/1982 and US\$1.0 billion in 1982/1983. A deficit of US\$4.7 billion is expected in the 1983/1984 fiscal year as a result of March 1983 oil price cuts and production quota.

To ride out the difficulties, in 1982/1983 the authorities drew heavily on the foreign exchange reserves that Indonesia had accumulated primarily during 1979 and 1980. The total foreign assets of the banking system fell from US\$11.3 billion in March 1982 to US\$9.1 billion at the end of the same year, and further declined to US\$8.8 billion at the end of February 1983. Large reductions in net foreign assets of the banking system during the last quarter of 1982 and the first quarter of 1983 were partly because of large capital outflows due to speculative pressures preceeding the latest devaluation. The March 30, 1983 devaluation, the second measures to minimize the current account deficit, has reversed the capital flow and rebuilt the foreign exchange assets of the banking system.

The government's decision to shelve, rephase and review its large projects was the third measure to narrow the foreign exchange gap. The rephasing of four major public sector projects alone saved more than US\$3 billion of budgeted foreign exchange expenditures in the 1983/1984 fiscal year.

The fourth step was to bolster the level of international borrowings. In January, 1983 the IMF announced that it had agreed to lend Indonesia SDR 69 million from the Indonesian contribution to IMF commodity buffer stock. In March, Indonesia obtained a US\$1 billion commercial loan through Morgan Guaranty Trust, another Yen 24 billion syndicated loan, and DFL100 million bonds issued in the Netherlands. From the IGGI, Indonesian obtained a new commitment of US\$2.2 billion in aid and loans for the 1983/1984 fiscal year. On March 1984, the government obtained a new loan of US\$750 million from a syndication of international banks.

According to a report by Morgan Guaranty Trust, Indonesia is now the seventh largest borrower in the world. By the end of 1982, the gross external debt of Indonesia was US\$24.4 billion. The report predicted that the total debt service ratio of Indonesia in 1982 year would be 28 per cent of total export. If the roll-over of short term debts are excluded, then the ratio becomes 14 per cent. Nevertheless, those ratios are much lower than those of the Latin American countries such as Argentina, Brazil, Chile, Mexico, Equador and Venezuela whose total debt service ratio already exceeds their respective annual export values. Those Indonesian figures are also below the debt service ratios of the Philippines, Thailand and Korea.

The past few years witnessed a gradual shift in Indonesia's sources of foreign borrowing. In the past, most of the foreign borrowing came from Of-

ficial Development Assistance (ODA), but since the Pertamina financial crisis in 1974/1975, the shares of commercial credits, syndicated loans and proceeds of bond floating in international markets have been increasing (Table 4). The terms of credit from ODA are much softer than those from other sources. The reason for this shift, apart from being a member of OPEC, is because Indonesia is no longer considered a poor country. With income per capita at US\$530 (1981) Indonesia now belongs to the middle income group, according to the World Bank's classification.

Table 4

INDONESIA'S FOREIGN BORROWING: NEW COMMITMENTS 1975-1982  
(US\$ million, current prices)

	1978	1979	1980	1981	1982	Average Terms 1981	
					(Est.)	Interest	Maturity (Years)
<i>Official development assistance</i>	<i>1,523</i>	<i>2,227</i>	<i>2,074</i>	<i>1,657</i>	<i>1,810</i>		
Bilateral Concessional	773	1,150	1,055	482	760	2.5	28.7
Multilateral	750	1,077	1,019	1,175	1,050	10.0	21.0
<i>Import related on "commercial" terms</i>	<i>373</i>	<i>1,133</i>	<i>1,011</i>	<i>2,778</i>	<i>2,140</i>		
Official	27	87	440	673	270	8.1	14.7
Buyers credits	305	817	449	883	940	7.4	11.7
Suppliers credits	41	229	122	1,222 <sup>a</sup>	930	6.9	9.6
<i>Untied borrowings</i>	<i>1,393</i>	<i>836</i>	<i>1,097</i>	<i>744</i>	<i>1,000</i>		
Financial institution <sup>a</sup>	1,295	773	1,052	704	1,000	15.5 <sup>a</sup>	10.0
Bonds	98	63	45	45	—	8.6	10.0
Total	3,288	4,197	4,182	5,184	4,950	8.6	15.0

<sup>a</sup> At variable rates.

Memo: LIBOR (The London Inter-Bank Offer Rate) averaged 16.5 per cent in 1981.

Source: World Bank Debtor Reporting System.

To improve the balance of payments position, and to reduce debt service ratios, the government intends to promote non-oil exports including tourism and export of manpower, reduce imports and step up the use of domestic products. As regards export of non-oil commodities, the measures the government has taken to pursue this objective are somewhat contradictory. The provision of concessional export credits, the establishment of export insurance, and devaluation are all beneficial to exporters. On the other hand, imposing quotas on exports of copra and palm oil has turned Indonesia into an unreliable

source of those products. The export counter purchase requirement on certain public sector contracts disturbs traditional marketing channels of Indonesia's own export commodities in international markets. Compulsory use of domestic products such as machinery, spare parts and raw materials might not have enhanced competitiveness of Indonesian goods in international market. This measure, along with the reservation of the exclusive rights to Indonesian shipping companies for shipment of government imports, has increased the cost of imports.

Port facilities need to be improved and customs procedures need to be simplified to step up non-oil exports. The industries themselves need structural adjustments in order to increase production and reduce costs. For example, capital utilization in plywood industry is now only around 50 per cent using two shifts of operation. Reducing excess capacity is not an easy task. The existing plants have to be restructured and infrastructure has to be established. Local labourers have to be trained to replace expatriates. Ocean going shipping lines and international markets for plywood are in the hands of few foreign multinational companies.

## MANAGEMENT OF FOREIGN EXCHANGE

Theoretically, since November 15, 1978 the external standard of the rupiah has been changed from its previous link to the U.S. dollar to a basket of currencies of Indonesia's trading partners. The currency composition of the basket and their weights are never disclosed by the authorities. By changing this standard, the variance of Indonesian real exchange rate is, theoretically, reduced and the impact of external terms of trade on domestic inflation is theoretically moderated.

Nevertheless, empirical evidence shows that the close links between rupiah and dollar remain after the last two devaluation. Rupiah rate to U.S. dollar is fairly stable compared to U.S. dollar rate to other major currencies. Because U.S. dollar is Indonesia's export currency, appreciation of it vis-à-vis other major currencies, caused a downturn in Indonesian import prices (mostly originating from Asia and Europe), while her export prices remained unchanged. On the other hand, depreciation of U.S. dollar increased the price of Indonesia's export bills (measured in U.S. dollar). In addition, the holding of U.S. dollar becomes more attractive in speculating for rupiah devaluation. As a result, the government depletes its holding of foreign exchange reserves in order to support the pegged rate.



## GOVERNMENT BUDGET

During the 1970s there was a rapid growth in the size of the government budget. Total revenue (in real terms) rose rapidly due to the two oil shocks in a decade. In 1969/1970 the first year of Pelita I, domestic revenue only equaled 9 per cent of GDP. Most of this came from indirect taxes on foreign trade. Ten years later in 1979/1980, at the beginning of Pelita III, domestic revenue had risen to 21 per cent of GDP (Table 5). In the 1979/1980 fiscal year, oil corporation taxes contributed 64 per cent of total domestic revenue, compared to only 20 per cent in 1969/1970. During the past decade, non-oil domestic revenue and foreign aid, as share of annual GDP during the period, remained

Table 5

GOVERNMENT REVENUE AND EXPENDITURE, 1969/70 - 1983/84  
(Rp billion)

	1969/70	1974/75	1979/80	1981/82	1982/83	1983/84 <sup>1</sup>
I. <i>Domestic Revenue</i>	243.7	1,753.7	6,696.8	12,213.6	12,418.3	13,823
Domestic revenue excluding oil	195.4	780.6	2,437.2	3,584.8	4,249.9	4,954
Oil corporation tax	48.3	973.1	4,259.6	8,629.8	8,170.4	8,864
II. <i>Expenditure</i>	309.4	1,827.0	8,076.0	13,917.7	14,335.9	16,565
III. <i>Deficit (II - I)</i>	65.7	93.3	1,379.2	11,705.1	1,937.6	2,742
IV. <i>Gross Domestic Product (GDP)</i> at current market prices	2,718.3	6,753	32,025.4	54,027 <sup>2</sup>	59,632.6 <sup>3</sup>	68,577.5 <sup>4</sup>
V. <i>Export price of Minas Oil</i> (US\$ 1 barrel)	1.67 <sup>5</sup>	12.60 <sup>6</sup>	21.12 <sup>7</sup>	35.0 <sup>8</sup>	34.53 <sup>9</sup>	29.53 <sup>10</sup>
VI. <i>As share of GDP (%)</i>						
Domestic revenue	8.9	26	20.9	22.6	20.8	20.2
Domestic revenue excluding oil	7.2	11.6	7.6	6.6	7.1	7.2
Oil corporation tax	1.7	14.4	13.3	16.0	13.7	13.0
Expenditure	11.4	27.1	25.2	25.8	24.1	24.2
Deficit	2.5	1.1	4.3	3.2	3.3	4.0

Sources: BPS, *Monthly Statistical Bulletin*, various issues.

Notes: <sup>1</sup>Budget figures.

<sup>2</sup>Revised figure.

<sup>3</sup>Preliminary figure.

<sup>4</sup>Estimates, assuming 15 per cent increases in nominal GDP in 1983/1984.

<sup>5</sup>As of January 1969.

<sup>6</sup>As of July 1974.

<sup>7</sup>As of July 1979.

<sup>8</sup>As of January 1981.

<sup>9</sup>As of November 1982.

<sup>10</sup>As of February 1983.

unchanged. The non-oil domestic revenue fluctuated around 7 per cent of GDP.

As the oil tax revenue boomed so did expenditures. The Government has maintained its balanced budget policy ever since Pelita I. The meaning of the balanced budget is that the budget deficit is financed by foreign aid and loans, which are classified as "development revenues." Foreign aid and loans contributed to between 3 and 4 per cent of GDP during Pelita I and II, in 1970/1971 the contribution of foreign aid and loans to total revenue was 26 per cent, but this declined to 17 per cent in 1979/1980. Total government expenditures increased to almost 26 per cent of GDP in 1981/1982 compared to 11 per cent in 1969/1970.

Because the government revenue is so dependent on oil tax receipts, stagnation in the price of oil, which happened for several years following the first oil shock, caused total spending to be curbed. Due to the oil glut in recent years, following the second oil shock in 1979, oil tax receipts in U.S. dollar have been falling well below the expected level. Without the March 1983 devaluation, the 1982/1983 and the present 1983/1984 budgets could not have been balanced. Since the tax bureaucracy has been unable to raise revenue at home to make up the shortfall in oil tax receipts, the only alternative has been to reduce government expenditures. In 1982/1983 the government expenditures were reduced to 24 per cent of GDP.

For the third successive year, in January 1984 the government raised the price of domestic petroleum products to reduce the burden of subsidies on the budget. Subsidies on fertilizers and pesticides were reduced while subsidies on certain food items were abolished. Wages of public servants were frozen in the 1983/1984 fiscal year and only increased by 15 per cent starting from April 1, 1984. A range of cost saving measures (such as reducing purchases of government vehicles, halting the construction of new buildings for various governments that had been scheduled for the 1983/1984 and 1984/1985 fiscal years) are also being implemented. These policies are intended to reserve as much as possible of the available resources for development program. Nevertheless, some of the development expenditures are actually not capital expenditures since they are salary supplements that should have been classified under "routine expenditures."

On tax policies, as from 15 November 1982, the government increased the departure tax from Rp35,000.00 per household to Rp150,000.00 per person, levied on residents of Indonesia. This tax is not related to the economic position of the taxpayer. A series of tax laws (the Income Tax Act, Value Added Sales Tax and Tax Procedures Act) came into effect on January 1, 1984 to replace the old ones, except for the tax on oil companies. The objective of the new

tax system is to increase tax revenues by broadening the tax base, hopefully to make up for the decline in oil tax revenues. The present tax system is simpler than the old one. Personal and corporate incomes are subject to the same tax rate. There is only three brackets, compared to 58 in the previous system. Those earning up to Rp10 million will be subject to a 15 per cent income tax rate. From Rp10 to Rp50 million the rate will be 25 per cent and above Rp50 million, 35 per cent.

There are many reasons why tax collection is low in Indonesia. First, people are reluctant to pay taxes since they have to pay levies fees, contributions and even bribes for services or documents they obtain from nearly all branches and layers of the government. Some of these collections are illegal and are not included in the budget. Second, the Indonesian legal and accounting system are still relatively undeveloped and therefore there is no way to measure the economic position of a taxpayer accurately and to enforce the regulations according to the letter of the law. Third, the taxation machinery is inefficient.

Tax collection is not only a function of the tax rate and tax base, but also of the efficiency, the ability and the honesty of the tax machinery. Tax reforms only deal with the tax rate, tax base and procedures. It will take a very long time to improve the legal and accounting system, to strengthen the tax machinery and to change people's behaviour, as well as to improve government services, before the government can collect substantial revenues from domestic taxes.

## MONETARY POLICY

As has been discussed in the previous section, since the oil price rise in late 1973, the government budget has become increasingly dependent on oil tax receipts and foreign aid and loans. These receipts do not reduce private domestic resources because they are transfers from foreigners. Oil tax revenues collected from domestically based foreign owned oil companies, for example, would otherwise have been repatriated abroad. These receipts and export taxes are received by the government in foreign exchange.

On the other hand, most of the government domestic expenditures are in Rupiah. This expenditure adds directly to domestic demand. In the present balanced budget policy, deficits in the domestic part of the budget (in Rupiah) are financed by surpluses in the foreign component of the budget (in foreign exchange). In other words, the government monetizes its receipts in foreign exchange to balance its budget. As a result, the money supply increased very rapidly the last decade (Table 6) while net foreign assets of the banking system



increased as well. This analysis shows that the structure of the government's budget and its policy to keep it balanced are the main sources of increases in money supply and hence in inflation.

To reduce inflationary pressures, Bank Indonesia, the central bank, has been using ceiling cum selective credit policies since April 1974 as instruments to control the expansion of total credits given by state owned banks and to direct the allocation of credits by economic sector, by race of the recipient and by the size of the company.

By definition, ceiling maintains status quo and therefore discourages competition among banks and between banks and other financial institutions. As a result, inefficient banks are protected from being overcome by the more efficient ones. The existing capital market segmentation is preserved, thus tending to prevent reduction of the costs of intermediation.

Selective credit controls involve the central bank more deeply with the state owned bank operations. To be effective, regulations on selective credit have to be more detailed. It is also necessary to organize an effective supervisory machinery since the problem of enforcement cannot always be left to conventional solutions. As a result, the state owned banks need more time and resources for uneconomic administrative work to verify customers dossiers and reports. In this kind of situation, bankers tend to be part of government bureaucracy and as a result more delay, uncertainty and other inefficiencies are expected and less credit can be handed out.

The recent partial liberalization of the state owned banks cannot and will not produce instant positive effects as over-staffing can not be solved overnight since firing people even though they are unproductive, is unpopular. Their portfolio structure, organization, and procedures need to be changed, and this takes time. Liberalization needs a different set of qualifications for the staff than is the case under a controlled system. A liberal system needs capable employees while a controlled system need subservient ones.

Loan rates have been subsidized at state owned banks and, for priority sectors, still are. At times, rates of interest are even lower than inflation rates during comparable periods. As a result, the recipients of credit are subsidized by simply obtaining credits from the state owned banks. Since the allocation of credits is not done through an interest rate mechanism, their allocation is similar to rationing.

Since the real rate of interest is arbitrarily fixed at a point which is negative and much lower than its equilibrium level, saving, investment and financial intermediation are sub optimal. As a result of subsidizing loan interest rates, for

example, low yielding investment activities became feasible, which would otherwise be unprofitable at positive equilibrium real interest rate.

The effectiveness of credit rationing to pursue the stated government objectives is questionable. In order for a selective credit policy to be effective, the degree of bank credit fungibility would have to be zero. Fungibility is defined as the ability of business firms to borrow credits for a particular purpose but use it for another. As the entrepreneurial sector in Indonesia is traditionally engaged in a variety of activities, business firms are likely to apply funds for various uses, according to their needs, not necessarily to the requirement imposed by the sources of the funds.

Since financing of their credits has been fully guaranteed by the central bank, the state owned banks have been almost constantly over-liquid. Because there was no need to mobilize funds, sometimes the state owned banks have refused to receive new time and saving deposits. During the last years of the last decade, the banks were encouraged to invest their over liquidity abroad. Since none of them has mastered the game in international markets, their overseas placements have been mostly in demand and short-term time deposits.

The present partial liberalization of the state owned banks, under which they can set their own deposit rates as well as lending rates for non priority economic sectors, will not produce immediate significant results either in mobilization of national savings or in a better allocation of resources. Because they have been fat cats for a decade, it will take time to build their capabilities to catch the mice.

Table 6 shows that rates of growth of the money supply have been consistently higher than inflation rates. This phenomenon can be partly explained by the increase in the demand for real balances due to increases in people's real incomes, and in the price level of non-essential goods. Another explanation is because the price of many items used in calculating the price indexes are controlled and subsidized by the government.

Except in 1973 to 1975 and 1979, the income velocity of money has tended to decline since Pelita I. In the course of economic development since 1969/1970, with structural changes and increasing urbanization and specialization, there has been an increase in market transactions at the expense of subsistence production. As a result, there has been an increase in the public's demand for real balances relative to output and thus to reduce the income velocity of money. The increase in velocity in 1973 to 1975 and 1979 were due to the oil shocks in those years that led to higher government expenditures, higher price expectations, and higher rates of inflation.

Table 6  
MONEY SUPPLY, GNP, INFLATION RATE AND  
INCOME VELOCITY OF MONEY, 1970 - 1983

Year	Money Supply (Rp billion)	GNP	Percentage Change In		Income Velocity of Money <sup>2</sup>
			Money Supply	Price Level <sup>1</sup>	
1970	241	3,290	34	8.9	—
1971	320	3,605	70	2.5	12.8
1972	474	4,405	48	25.8	11.1
1973	669	6,508	41	27.3	13.4
1974	937	10,201	40	33.3	10.9
1975	1,250	12,087	33	19.7	11.0
1976	1,603	15,035	28	14.2	10.5
1977	2,006	18,332	25	11.8	10.1
1978	2,488	21,606	24	6.9	9.6
1979	3,385	30,541	36	21.8	10.4
1980	4,995	41,435	48	16.0	9.9
1981	6,486	52,102 <sup>3</sup>	30	7.1	9.0
1982	7,121	57,675 <sup>4</sup>	10	9.9	8.5
1983	7,569	66,326	6	11.5	9.0

Sources: 1. Bank Indonesia, *Weekly Report*, various issues.  
2. Biro Pusat Statistik, *National Income of Indonesia (Main Tables)*, various issues.

Notes: <sup>1</sup> The Jakarta Cost of Living Index through 1978 and the Consumer Price Index for Indonesia (Composite of 17 cities) thereafter.  
<sup>2</sup> Income velocity of money =  $Y_t / \frac{1}{2} (M_{t-1} + M_t)$ .  
<sup>3</sup> Revised figures.  
<sup>4</sup> Preliminary figures.

CONCLUSION

Whether the government can maintain the momentum of development and attain the 5 per cent growth rate in Pelita IV, depends upon its ability to compensate for the decline in oil taxes by mobilizing domestic resources through taxation and the banking system. Since development needs foreign exchange financing, the government ability to step up non-oil exports is also crucial. All forecasters predict that even though the nominal price of oil will continue to rise in this decade, in real term it is going to decline.

The first year after partial liberalization of the banking system witnessed a dramatic change in the composition of deposits at state owned banks. Their



holdings of time deposits with maturities of up to one year has been increasing at the cost of a declining trend in demand deposits with a maturity of 24 months. This evidence shows that bank customers do change their structure of portfolios as a reaction to the changes in the term structure of interest rates that had been brought about by the partial liberalization in the banking system. The outstanding position of overall time deposits with state banks increased from Rp911.8 billion (May 1983) to Rp1,581.7 billion (September, 1983), an increase of more than fifty per cent in less than four months.

Theoretically, mobilization of savings through the banking system can be increased as long as it is convenient, it is simple, it is safe, and as long as it offers a satisfactory return for savers. The savings rate in Indonesia is quite high. For example, an analysis of Susenas data (National Expenditure Survey) suggests that in rural areas, households save on average about 20 per cent of their income. Unfortunately, only a small fraction of that enters the formal financial system.

Mobilization of savings through the banking system can also be increased by making the payment of most of government's transactions (including civil servants' salary) through the banking system compulsory, that is by using checks that can be cashed at any bank. Another measure would be to increase the ratio of monetization of economy, that is, to increase the volume of money relative to national product, before spilling over into inflation. Currently, the ratio of money, in its broad definition, to GDP in Indonesia (19 per cent) is much lower than in Malaysia (53 per cent), in India (28 per cent), or in Nigeria (28 per cent). To increase the degree of monetization of GDP, the number of branch offices of the banks should be increased and public relations campaigns by the banks should be intensified because many people do not know about the advantage, purpose and functions of a bank and a banking system.

Extending of loans encompasses a totally different set of issues from savings mobilization. The latter is concerned intimately with incentives for saving. The first relates to the bank's transaction cost and its perception of efficiency of the loan market. Transaction cost is the administrative cost per unit of loan. Efficiency of the loan market relates to the bank's perception of uncertainty with regard to the productive return of the project that is financed by the credit, and the ability of the bank to select honest borrowers and projects that give greater returns.

Ceiling cum credit policies with subsidized loan interest rates has increased the transaction costs of the state owned banks. High default rates on their credits shows their inefficiency in extending loans. These reasons along with the current economic downturn have slowed credit expansion of the state owned banks after liberalization.

A monetary policy can be used as a useful tool in restoring external balance at minimum costs in lower domestic economic activities. As has been discussed in section 1, however, there is a dilemma in pursuing these objectives. To prevent capital out-flow and a surge in domestic inflation, a relatively tight credit policy is needed in order to increase the prevailing interest rates. On the other hand, domestic economic units need cheap working capital to finance higher import prices (after March 30, 1983 devaluation) and to finance their increased inventories during the present depressed demand. Restructuring of the existing industrial capacity also needs additional investment. Until now, the government seems to be more concerned about restoring external balance at the cost of unnecessary cutbacks in domestic output.

To achieve the more important economic objectives of the government in the mobilization of domestic savings, better allocation of economic resources, and promoting non-oil exports, the present discrimination on private owned banks should be relaxed. Small domestic banks, which traditionally serve small firms and small savers, should be encouraged to increase their participation in the mobilization of small savings as well as in channelling credits to this class of customers. Expertise of foreign banks should be used to expand non-oil exports. There is a little doubt that they have more experience in dealing with the financing of export counter purchases, than state owned banks have. For these reasons, these banks should have more access to rediscount facilities at the central bank.

To reduce pressures on the government budget, government investment through state owned enterprises have to be reduced and reviewed. The state owned enterprises should be encouraged to mobilize funds through capital markets, as successfully done by PT Jasa Marga, a toll road public company. New public investment has to be concentrated on the provision of public goods and leave more of the production of private goods to the private sector. The public companies need to be re-dressed and strengthened in order to make them agents of development, or at least not burdens to society.

Decontrol, deregulation and other non-interventionist programs are necessary to place more reliance on market forces in order to create an environment in which businessmen can operate without too much direct interference from the government bureaucracy. The existing pricing and industrial policies, and licensing procedures for investment and for trade have become too burdensome for the economy and production as well as the export promotion of non-oil commodities.

# Indonesia's Economy in Pelita IV

Pande Radja SILALAH

## INTRODUCTION

As of 1 April 1984, Indonesia entered the fourth stage of its development endeavours. Unlike the situation prior to Pelita III (the Third Five-Year Development Plan), the economic situation during the last two years of Pelita III was not bright. Indonesia's economic growth in 1982 only reached 2.25 per cent and in 1983 it was not very different from that of the previous year.

On 9 January 1984, the government forwarded Pelita IV to Parliament and in that plan the Indonesian economic growth has been set at the average of 5 per cent per year. It appears that the targeted economic growth will most likely be achieved if the economy is managed in a better way.

Experience has shown that the inability to anticipate, the sluggishness to act and react, and the tardiness in taking initiatives have adverse impact on development efforts. All of them need not to reoccur for the challenge to be faced in Pelita IV will be increasingly more complex and complicated, although it is said that Indonesia's economists will become geniuses in case of emergency.

In the last few months there are indications that the economy of industrial countries, particularly the U.S., has been recovering so that those countries may be expected to function as the "locomotive" of the world economy including that of Indonesia. Since, however, up to now there has not been any convincing guarantee that the aforementioned locomotive might be able to advance smoothly, alertness is still a *conditio sine qua non*. In the present condi-



tion of the world economy speed to act systematically will be decisive in determining to what extent the existing opportunities can be exploited for Indonesia's economic development.

To achieve the expected economic growth rate, in the directives of Pelita IV are stipulated the steps to be taken by the government including that of solving the existing problems. However, in order to have a clearer picture, some issues that need to be given serious attention will be discussed in this analysis. Those problems are put forward and need to be discussed because Indonesia's success to attain the economic growth rate as referred to earlier depends to a large extent on her ability to solve the problems mentioned above. Those problems are consecutively as follows: foreign trade, balance of payments, dependence on foreign aid, employment opportunities, taxation and the role of the private sector.

## FOREIGN TRADE

Indonesia which adheres to an open economy, is willy nilly not excepted from the impact of the world economic recession. The global trade development will directly affect Indonesia's international trade and the extent of the impact greatly depends on the exposure of Indonesia's economy to the global one. Statistical data reveal that the ratio of export plus import to the Gross National Product in 1969 only amounted to approximately 29.69 per cent, but in 1982 it reached 57.17 per cent. This means that Indonesia's economy is more open to the outside world so that by itself she is more sensitive to the development and fluctuations of international trade.

From the data in Table 1 it can be noted that from the onset of Pelita I up to the third year of Pelita III Indonesia's export increased considerably. In fiscal year 1969/1970 its export value only amounted to US\$1,044 million, and in fiscal year 1981/1982 it reached the sum of US\$23,606 million, which is an increase of approximately 29.68 per cent annually. But due to the world economic recession compounded by the decline of the oil prices, Indonesia's exports dropped considerably. The impact of the global economic slump has been increasingly felt by Indonesia's economy for to date a substantial part of Indonesia's exports has been directed towards some specific countries only. During the last few years about half of Indonesia's exports was directed to Japan, almost one-fifth to the U.S., around one-twentieth to the EEC member countries and only one-eighth went to the ASEAN member countries.

Further observation has shown that during the period of 1969/70 - 1981/82 the export growth of oil and gas was much higher than that of non-oil and gas. During that period the export of oil and gas increased more than 50 times while

Table 1

INDONESIA'S EXPORTS AND IMPORTS 1969/1970 - 1983/1984  
(million US\$)

	Export (f.o.b.)			Import (c.i.f.)		
	Oil & Gas	Non-oil & Gas	Total	Oil & Gas	Non-oil & Gas	Total
1969/1970	384	660	1,044	88	1,139	1,227
1970/1971	443	761	1,204	94	1,138	1,232
1971/1972	590	784	1,374	132	1,249	1,381
1972/1973	965	974	1,939	159	1,661	1,820
1973/1974	1,078	1,095	3,613	461	2,938	3,399
1974/1975	5,153	2,033	7,186	1,275	4,341	5,616
1975/1976	5,273	1,873	7,146	930	5,090	6,020
1976/1977	6,350	2,863	9,213	1,753	6,167	7,920
1977/1978	7,353	3,507	10,860	1,490	7,241	8,731
1978/1979	7,374	3,979	11,353	1,883	7,543	9,426
1979/1980	11,649	6,171	17,820	3,534	9,097	12,631
1980/1981	16,883	5,587	22,470	5,255	11,913	17,168
1981/1982	19,436	4,170	23,606	5,497	14,336	19,833
1982/1983	14,976	3,893	18,869	4,559	15,048	19,607
1983/1984*	14,332	4,750	19,072	4,524	14,400	18,924

\*Estimated figure.

Source: The 1984/1985 Draft State Budget.

that of non-oil increased only at about 6.3 times. This indicates that Indonesia's exports depend to a large extent on oil. On the other hand, it turned out that the non-oil export commodities are still less varied or only rely on some kinds of commodity.

In line with the export, Indonesia's import also increased considerably. At the beginning of the fiscal year of Pelita I the overall import only amounted to US\$1,227 million, and in fiscal year 1981/1982 it amounted to US\$19,883 million which means that the average annual increase is 6.10 per cent.

Further observation also shows that although the export growth rate was higher in nominal terms than that of imports, based on the 1973 constant price, during 1969-1982 the imports increased 7.82 times while the export of goods and services increased 1.94 times only. Based on a rough estimate from the data, it can be noted that the income elasticity of import stood at about 2.40 at the 1973 constant price, and the income elasticity of export only reached the figure slightly above 0.70. This illustration reveals that Indonesia's economic growth increasingly depends on imports. The composition of im-



ports gives a picture which is not so advantageous to Indonesia. From the data in Table 2 it can be noted that the import share of raw materials and capital goods tend to increase. In 1971 the import share of raw materials and capital goods in the total imports only reached 38.81 per cent and 42.13 per cent respectively. But in 1982 it reached 44.26 per cent and 48.27 per cent respectively.

Table 2

## IMPORT VALUE BY COMMODITY (value c.i.f., million US\$)

Year	Consumer Goods		Basic/Aux. Material		Capital goods		Total	
	Value	Share	Value	Share	Value	Share	Value	Share
1971	210.2	(19.06%)	428.6	(38.81%)	464.6	(42.13%)	1,102.8	(100%)
1972	251.8	(16.12%)	597.7	(38.27%)	712.2	(45.67%)	1,561.7	(100%)
1973	648.7	(23.77%)	973.2	(35.66%)	1,107.2	(40.57%)	2,729.1	(100%)
1974	707.0	(18.40%)	1,582.2	(41.19%)	1,552.6	(40.41%)	3,841.9	(100%)
1975	677.5	(14.20%)	1,961.1	(41.12%)	2,131.2	(44.68%)	4,769.8	(100%)
1976	915.9	(16.14%)	2,024.1	(35.68%)	2,738.1	(48.18%)	5,673.1	(100%)
1977	1,104.6	(17.73%)	2,452.5	(39.36%)	2,673.2	(42.91%)	6,230.3	(100%)
1978	1,196.6	(17.88%)	2,664.5	(39.83%)	2,829.3	(42.29%)	8,690.4	(100%)
1979	1,182.7	(16.42%)	3,327.5	(46.20%)	2,692.1	(37.38%)	7,202.3	(100%)
1980	1,543.4	(14.25%)	4,807.6	(44.37%)	4,483.4	(41.38%)	10,834.4	(100%)
1981	1,398.7	(10.54%)	5,700.8	(42.95%)	6,172.6	(46.51%)	13,272.1	(100%)
1982	1,259.8	(7.47%)	7,461.2	(44.26%)	8,137.9	(48.27%)	16,858.9	(100%)

Source: Central Bureau of Statistics, *Import by Commodity and Country of Destination*, 1981 and *Economic Indicator*, September 1983.

It is obvious that the composition of export and import presented above cannot be maintained and serious efforts should be made to change it so as to enable Indonesia's economy to reach the expected growth rate and concurrently become more resilient. In Pelita IV it can almost be ascertained that there will be no more spectacular increase in oil export as was the case during the previous years. Hence continuous attention need to be given to the increase of non-oil export. The will and sincerity of the government together with the business community cannot be doubted and this was really proven by the series of measures taken such as devaluation, extension of credit with low interest rate and better cooperation between the government and private entrepreneurs.

Experience reveals to us that in the effort to promote export the problems to be faced by Indonesia are not only restricted to the demand constraint. From the devaluation in November 1978 and that of March 1983 it has become increasingly clearer that one of the constraints that has to be overcome is that



of supply. This supply constraint has something to do with the supply of commodity to be exported by various kinds that can be distributed to consumers in a smooth and regular manner according to the needs. This problem may be solved properly if aside from other efforts industrialization be linked to promoting export.

To promote export, the government has attempted to simplify and facilitate the complicated procedures. These efforts should be intensified since according to business people, one of things that haunts them most is the complexity of the procedures that has to be gone through. On the other hand this factor may increase the costs or even disable them to meet the demands previously agreed upon. If this problem cannot be solved in a more proper manner in Pelita IV, it will be very difficult to achieve optimum results.

It has been pointed out earlier that the composition of Indonesia's imports is not so favourable and attempts to improve it seemed to be somewhat difficult especially because efforts to curtail imports may lead to the decline of economic growth. The outcome of the industrial census in 1981 shows that the import content (covering only raw materials) of the overall industrial sector reached 37.5 per cent. Up till now it is often said that Indonesia is rich in raw materials which are ready to be processed. But the reality seems to be different. It turns out that there has not been as yet any serious effort to process the existing raw materials or resources.

It is laid down in Pelita IV that the import of goods (f.o.b.) is to be promoted at the rate of 7.87 per cent annually and this is to comprise 5.76 per cent of oil, 15.26 per cent of LNG and 8.39 per cent of non-oil import increase. Further, the increase of non-oil import is to comprise 1.48 per cent of consumer goods, 6.79 per cent of raw materials and 11.76 per cent of capital goods. Related to the income elasticity of import during the period of 1971-1982, apparently serious efforts will be made to lower the import growth rate; and to meet domestic needs, it is expected that domestic production can play a significant role. The problem is of course whether domestic production can meet the needs (particularly raw materials and capital goods) economically. This should be taken into account lest efforts to lower the import become a boomerang in the form of the establishment of in-efficient industries, which are unable to compete with foreign production or the slowing down of production activities.

It is most likely that many industrial enterprises import the needed raw materials from abroad and many companies are not interested to produce certain commodities, because they do not know that those raw materials are produced domestically or those commodities find markets in the country. Such gaps should be tackled, and even efforts to encourage domestic producers to

use home-made products "in a healthful manner" and to stimulate them to produce the needed commodities in a well-directed way should be promoted. In other words, efforts to create and/or to strengthen inter industrial linkages need to be intensified. Indonesia has at present a junior minister for the promotion of the use of domestic products. With this institution, it is expected that it would be easier to create and develop linkages, both forward and backward, of the existing industries.

With the establishment and operation of the new oil refineries, the pressure from the inflated oil import can be alleviated. Nevertheless, it does not follow that the handling of imports will be easier. The problem of directing imports in Pelita IV has become increasingly difficult and complex and consistent as well as well-oriented actions are called for.

## BALANCE OF PAYMENTS

Toward the beginning of Pelita IV, some rumours related to the economy sprang up and spread, which in turn made some people panicky and even threatened the smooth running of the economic activity. The latest rumours were those on devaluation by the wake of 1983. After some study it turned out that those rumours which had caused much anxieties were centred around the issue on the balance of payments. During the two initial years of Pelita III, in the current transactions Indonesia still experienced a surplus, but since fiscal 1981/1982 there has been a deficit. The swelling of the deficit in fiscal 1982/1983 caused many people begin to speculate that the government would face difficulties in the balance of payments and that the position of foreign exchange reserves could no longer guarantee the continuation of economic activities (import) in an appropriate manner (see Table 3).

With the devaluation of 30 March 1983 and the subsequent adoption of the policy in the banking sector, the rescheduling of some government's projects, the Current Balance of Payments can be improved although it was still in a deficit position. According to an estimate, although exports (f.o.b.) may be increased to slightly above 9 per cent each year and imports may be increased by less than 8 per cent during Pelita IV, Indonesia's current transactions may continuously experience a deficit amounting to approximately US\$5 billion every year. This means that without foreign aid and foreign capital inflow to balance it, Indonesia's balance of payments will be in a difficult position and its foreign exchange reserves will be exhausted.

Based on such a trend, one may say that in the coming five years more intensive efforts will be made to attract foreign investment. And in Pelita IV Indonesia should be more open to foreign investment.



Table 3

## BALANCE OF PAYMENTS 1978/1979 - 1983/1984 (US\$ million)

	1978/1979	1979/1980	1980/1981	1981/1982	1982/1983	1983/1984*
1. Goods and Services						
1. Export, f.o.b.	+ 11,353	+ 17,820	+ 22,470	+ 23,606	+ 18,869	+ 19,072
Oil	+ 7,374	+ 11,649	+ 16,883	+ 19,436	+ 14,976	+ 14,322
Non-oil	+ 3,979	+ 6,171	+ 5,587	+ 4,170	+ 3,893	+ 4,750
2. Import, c & f	- 9,426	- 12,631	- 17,168	- 19,833	- 19,607	- 18,924
Oil	- 1,883	- 3,534	- 5,255	- 5,497	- 4,559	- 4,524
Non-oil	- 7,543	- 9,097	- 11,913	- 14,336	- 15,048	- 14,400
3. Services	- 3,082	- 3,612	- 4,863	- 6,043	- 5,871	- 5,206
Oil	- 1,481	- 1,675	- 2,539	- 3,487	- 3,218	- 2,793
Non-oil	- 1,601	- 1,937	- 2,324	- 2,556	- 2,653	- 2,413
4. Current Transaction	- 1,155	+ 1,577	+ 439	- 2,270	- 6,609	- 5,058
Oil	+ 4,010	+ 6,440	+ 9,089	+ 10,452	+ 7,199	+ 7,005
Non-oil	- 5,165	- 4,863	- 8,650	- 12,722	- 13,808	- 12,063
II. SDR	+ 64	+ 65	+ 62	—	—	—
III. Government Capital Inflow	+ 2,101	+ 2,452	+ 2,698	+ 2,853	+ 4,114	+ 6,971
1. Program Aid	+ 94	+ 196	+ 150	+ 6	+ 21	+ 97
2. Project Aid and Others	+ 2,007	+ 2,256	+ 2,548	+ 2,847	+ 4,093	+ 6,874
IV. Other Capital Flows	+ 392	- 1,358	- 361	+ 1,140	+ 1,397	+ 676
V. Debt Settlement	- 632	- 722	- 617	- 861	- 949	- 988
VI. Total of I to V	+ 770	+ 2,014	+ 2,221	+ 862	- 2,047	+ 1,601
VII. Unaccounted difference	- 62	- 324	+ 515	- 1,850	- 1,232	+ 110
VIII. Monetary Flow	- 708	- 1,690	- 2,736	+ 988	+ 3,279	- 1,711

\* Estimated realization.

Source: The 1984/1985 Draft State Budget.

One of the chronic diseases of Indonesia's balance of payments is the transaction of services particularly of transportation and travel which always experience deficit. If at the beginning of Pelita I the deficit of travel and transportation only amounted to US\$173 million in fiscal 1982/1983 it stood at US\$2,656 million. As it stands now the position of the balance of travel and transportation should be improved as soon as possible. With the issuance of the Presidential Decree No. 18 of 1982 it was expected that the situation would improve. But actually the sea transportation sector has not developed properly until now so that more serious attention should be given to improve it. Giving priority to this sector seems well founded since through those efforts it is expected that the smooth flow of goods may also be improved. Thus Indonesia should step up the capability of its national fleet through renovating the means of transportation and adjust them to the kinds, nature and volume of the transported goods. This kind of action needs to be taken soon because in a situation where many shipping companies are facing difficulties the aforementioned efforts are easier to be made.



## DEPENDENCE ON FOREIGN AID

Since the beginning of Pelita I loans or foreign aid has played a role in Indonesia's economic activities. Seen from the perspective of quantity, foreign aid has continuously increased. If at the beginning of Pelita I the total of foreign aid only amounted to US\$371 million, in the last year of Pelita III, according to an estimate, it amounted to US\$6,971 million. Cumulatively during three Pelitas the sum total of foreign aid amounted to US\$30,037 million and it is expected to continuously increase during Pelita IV. By calculating the total of interests and debt installments during three Pelitas (see Table 4) it can be estimated that the government's debts up to the end of Pelita III totaled at about US\$25 billion, in which the debts made by the Old Order are not included.

Table 4

GOVERNMENT'S CAPITAL INFLOW, INTERESTS AND DEBT INSTALLMENTS  
(million US\$)

	Inflow Government Capital	Cumulative	Interests and Debt Installments	Cumulative
1969/1970	371	371	31	31
1970/1971	369	740	47	78
1971/1972	400	1,140	78	156
1972/1973	481	1,621	66	222
1973/1974	643	2,264	81	303
1974/1975	660	2,924	89	392
1975/1976	1,995	4,919	77	469
1976/1977	1,823	6,742	166	635
1977/1978	2,106	8,848	761	1,396
1978/1979	2,101	10,949	632	2,028
1979/1980	2,452	13,401	722	2,750
1980/1981	2,698	16,099	617	3,367
1981/1982	2,853	18,952	861	4,228
1982/1983	4,114	23,066	949	5,177
1983/1984*	6,971	30,037	988	6,165

\* Estimated figures.

Source: The 1984/1985 Draft State Budget.

This continuous increase of foreign aid has brought about concern to some people. Today the opinion that Indonesia is becoming more and more dependent on foreign countries has increasingly gained the ears of the people. The problem of repaying debts has been ever more widely discussed in its links to that of the balance of payments and debt service ratio.

The data in Table 5 shows that at the beginning of Pelita I, foreign aid played a very significant role in Indonesia's economy and particularly in the State Budget. In fiscal 1969/1970 approximately 77 per cent of the development funds derived from foreign aid. But in the following years the portion of foreign aid decreased significantly, so that in Pelita III it stood at less than 30 per cent in the overall development fund. But during Pelita IV it is expected that the portion of foreign aid in the development funds will be larger than that in Pelita III, and this means that Indonesia's dependence on foreign countries will be greater again. On the other hand it can be estimated that investments deriving from foreign aid may range from 18 per cent to 24 per cent of the whole investment.

Table 5

SOURCES FOR THE FINANCE OF DEVELOPMENT BUDGETS  
(Rp billion)

	Government Savings (1)	Foreign Aid Funds (2)	Total Development Fund (3)	(2)/(3) % (4)	Total State Budget Income** (5)	(2)/(5) % (6)
1969/1970	27.2	91.0	118.2	77.0	334.8	27.2
1970/1971	56.4	120.4	176.8	68.1	465.1	25.9
1971/1972	78.9	135.5	214.4	63.2	563.5	24.1
1972/1973	152.5	157.8	310.3	50.9	748.4	21.1
1973/1974	254.4	203.9	458.3	44.5	1,171.7	17.4
1974/1975	737.6	232.0	969.6	23.9	1,985.7	11.7
1975/1976	909.3	491.6	1,400.9	35.1	2,733.5	18.0
1976/1977	1,276.2	783.8	2,060.0	38.0	3,689.8	21.2
1977/1978	1,386.5	773.4	2,159.9	35.8	4,308.8	18.0
1978/1979	1,522.4	1,035.5	2,557.9	40.5	5,301.6	19.5
1979/1980	2,635.0	1,381.1	4,016.1	34.4	8,077.9	17.1
1980/1981	4,427.0	1,493.8	5,920.8	25.2	11,720.9	12.7
1981/1982	5,235.0	1,709.0	6,944.0	24.6	13,921.6	12.3
1982/1983	5,422.0	1,940.0	7,362.0	26.4	14,358.3	13.5
1983/1984*	6,548.5	2,741.0	9,290.3	29.5	16,565.4	16.6
1984/1985	6,048.3	4,411.0	10,459.3	42.2	20,560.4	21.5
1985/1986	8,072.5	5,098.0	13,170.5	38.7	25,068.8	20.3
1986/1987	9,756.9	5,715.3	15,472.2	36.9	29,396.4	19.4
1987/1988	11,427.8	6,686.8	18,114.6	36.9	35,005.9	19.1
1988/1989	13,048.0	7,475.5	20,523.5	36.4	41,017.3	18.2

\* Estimated figures.

\*\* Including the balance of the budget surplus. Repelita IV figures since 1984/1985.

Source: The 1984/1985 Draft State Budget.

Viewed from its significance, as referred to earlier, one may say that foreign aid is still complementary so that it is not against GBHN (the Broad Guidelines of the State Policy). Nevertheless, serious attention should be given to the management of that aid. In the 1984/1985 State Budget put forward by the government some time ago, the post of interests and foreign-debt installments shows a significant increase. This reveals that the maturity date of the previous debts has begun to be in effect. Accordingly if the debts schedule is not properly set, Indonesia's position will increasingly become difficult.

Recently the problem of debt service ratio has been widely discussed. According to the government's statement Indonesia's debt service ratio has exceeded the figure of 20 per cent -- the ceiling which is considered safe. From the analyses and discussions on this problem one can say that most observers tend to focus their attention on the 20 per cent ceiling. History shows that some countries have been successful in their economic development although their debt service ratio has exceeded by far the 20 per cent ceiling. This means that the most important factor is whether the country concerned is capable of utilizing the acquired funds efficiently and effectively, in the sense that the funds yield bigger real result compared with the price to be paid without adversely affecting the economy. Thus it stands to reason that attention should be given to the use of those funds properly in Pelita IV. As referred to earlier, the role of foreign investment will be greater in Pelita IV than in Pelita III. Hence the acquired funds should be properly managed. If that is the case one needs not fear that foreign aid or capital may play a dominant role and chauvenistic attitude with all its manifestations cannot be overcome.

A study on foreign capital reveals that foreign capital investments in Indonesia have the following characteristics: (1) capital intensive; (2) the marketing of products is oriented towards meeting the needs of domestic markets; and (3) with activities to look for basic raw materials. This tendency should be gradually changed in Pelita IV. Foreign capital should be directed in such a way so as to be able to sustain industrialization endeavours (to restructure the economy, to make the industrial sector resilient); to absorb more labourers; and to be more oriented towards international market. The latter should be given serious attention lest in Pelita IV the competition for domestic market between national and foreign entrepreneurs exacerbates.

## EMPLOYMENT OPPORTUNITIES

In the Repelita IV book it is pointed out that during the period of 1971-1980 employment opportunities increased sharply, namely by 0.3 per



cent annually. This growth exceeds that of the population aged 10 years and above and of the labour force which is each 2.9 per cent. Meanwhile it is also mentioned that the labour force in 1983 stood at 63,475.9 thousand and in 1988 it will have amounted to 72,796.1 thousand. This means that during Pelita IV there will be a new labour force increase of 9,320.2 thousand or an average increase of 2.78 per cent annually. During the period of 1971-1980 Indonesia's GDP at constant 1973 prices increased at an average of 8 per cent annually, consequently the employment elasticity during that period stood at about 0.375.

Some empirical studies have shown that generally employment elasticity tends to decline with the increase of production of the society. This is due to the fact that the production activities are capital intensive rather than labour intensive. This kind of process seems likely to occur in Indonesia as well. Should this be the case it can be concluded that without taking special measures related to employment in Pelita IV, the increase of new labour force cannot be absorbed through new work opportunities and consequently there will be more un-employment.

In Pelita IV, the government expects that the total increase of labour force will be absorbed. This expectation is too optimistic and with it the government implies that the elasticity of the labour force actually increases from 0.375 to approximately 0.556. Theoretically, if it is not an illusion, it is possible but in practice it does not seem very likely to happen.

The unemployment increase will certainly bring about and/or exacerbate social problems, such as the increase of labour disputes, criminal behaviour, which may in turn arouse social restlessness. This means that in Pelita IV, aside from efforts to tackle social problems brought about by the increase of unemployment, efforts to deal with the roots of the problem should be made. Based on the labour force trends referred to earlier one may say that in Pelita IV efforts to mobilize the available funds, particularly those managed by the government, for labour-intensive projects and for projects that are able to curb the increase of people looking for jobs, such as education and training, need to be intensified. Without particular efforts to mobilize funds it can be ascertained that the pressure of the employment problem will grow and consequently may hamper the smooth process of development.

## TAXATION AND THE ROLE OF THE PRIVATE SECTOR

It is a fact that the prime mover of Indonesia's economic growth is the public sector. In fiscal 1983/1984, for example, although the government's

share in the economic activity (ratio of the total revenue and expenditure of the government to the GNP) was around 23 per cent, the government's share in the total investments (deriving from government savings and foreign aid) was more than 55 per cent. The rise of oil prices and production during the previous years gave the opportunity to the government to increase expenditure (investments) without directly imposing a significant burden on the public through taxation. In Pelita IV this kind of policy can no longer be maintained because it would be difficult to increase the government's income from the oil sector in a spectacular way. To maintain and/or to create economic growth through investments the government apparently will intensify revenues from taxes and participation of the private sector.

Last December 1983 the Bills on Taxation presented by the government were approved by the DPR (Parliament) and would be effective in 1984. With the enactment of the new Tax Laws it is expected that the government's revenues from the tax sector can be increased although during the first years it may technically still face difficulties or constraints. Increasing revenues from the tax sector by levying progressive taxes may in many aspects cause the private sector move in opposite directions. This will most likely happen particularly in developing countries because a substantial part of the private investments are derived from big entrepreneurs. In Pelita IV, efforts will be made to increase revenues from taxes in line with the increase of private investments. In order to be successful in such endeavours the practice of "hunting in the zoo" in the field of taxation has to be quickly abandoned, and serious efforts to raise the number of taxpayers should be made. It is expected that such an endeavour may be successfully carried out because up to now the number of taxpayers is very small and even too small and the burden of taxes imposed on the people is still not too heavy.

In any country tax embezzlements always happen and a compromise between the tax collector and taxpayer is a case in point which is not unfrequent. Theoretically, there will be more tax embezzlements when taxpayers do not feel the benefit of paying taxes or feel that the cost to illegal compromise is smaller than the sum they can embezzle. The former problem may be solved if the funds deriving from taxes are utilized according to the expectation of the taxpayers (the public). As to the latter problem it can only be solved if matters concerning taxes are properly managed and the mentality of tax collectors can be relied upon. To date we have often heard complaints of the people on the behaviour of the tax apparatus. The government itself has explicitly announced to take appropriate measures for improvements. It is expected that this determination will be realized in Pelita IV. As is common knowledge, with the ever increasing burden of taxes in Pelita IV, the public will be more sensitive and critical towards matters concerning taxation.



## CONCLUSION

The world economy has shown symptoms of recovery from its recession and will completely recover although it still remains to be seen whether this condition will continue. This good prospect has certainly open possibilities for Indonesia to continue the development endeavours as expected. In Pelita IV Indonesia expects to reach an average economic growth of 5 per cent per year. This expectation may be realized but to this end real efforts should be made and serious handling of issues that may arise would be needed.

At the beginning of Pelita III the economic condition of Indonesia and the world was quite good, but toward and in Pelita IV many factors need to be tackled seriously. This is mainly due to the fact that problems to be faced have increasingly become complicated and complex. In the past many development endeavours did not reach the optimum result due to inability to anticipate, sluggish action and reaction, and slowness in taking initiatives. This kind of situation can no longer be maintained because Indonesia's capability to achieve the expected results of its economic development greatly depends on its ability to solve the existing problems properly in accordance with their urgency.

In Pelita IV, it seems very likely that problems of foreign trade, balance of payments, dependence on foreign aid, employment opportunities, taxation and the role of the private sector will come to the fore. Those problems have to be properly solved in Pelita IV so as to facilitate the achievement of the development objectives according to the GBHN (the Broad Guidelines of the State Policy).



# **The Expansion of the Role of the Private Sector during Pelita IV: between Urgency and Reluctance**

Djisman S. SIMANDJUNTAK

Among the changes expected by the government to take place during Pelita IV (Fourth Five-Year Development Plan) there is the expansion of the role of the private sector within national economic development. Indications of this change can be seen among other things in the composition of national investment planned. During Pelita IV private investment is expected to increase at the rate of 17.6 per cent per year from Rp8.7 trillion in 1984/1985 to Rp19.5 trillion in 1988/1989. Surely public investment is also planned to keep increasing. But its growth rate is only 14.4 per cent per year so that public investment (government development expenditures) will amount to Rp20.5 trillion in 1988/1989, or 51.3 per cent of national investment as compared with 54.7 per cent in 1984/1985. Certainly, one does not know as yet the share of the private enterprises in the whole private investment which also includes these investments undertaken by state enterprises. But statements issued by the government show that the private enterprises are expected to become an important pillar in realizing the private investment. This is the first indicator of the will to expand the role of the private sector in economic development.

Some government regulations in recent years have also expressed that will. From the instruments contained in the Export Promotion Policy of 1 January 1982 can be mentioned the transition to the system of *free foreign exchange* from that of directly controlled one. Under this regulation, holders of foreign exchange are given freedom to get the most from their foreign exchange. The obligation to exchange foreign exchange at the Bank Indonesia at the administrative rate has been abolished. That way the Indonesian system of foreign exchange has become very rich with alternatives.

This change in the system of foreign exchange has great consequences for Indonesia's fiscal and monetary policies. Supposing there is an indication that the domestic value of the rupiah will drop while its external value does not change or drops more slowly, or in other words, there is a trend of overvaluation of the rupiah, capital export can take place, while capital import becomes rare, meaning a decrease in monetary reserves. The difference between real domestic and foreign interest rates can push capital outflows as well which are not wanted by the monetary authorities. The experience during the last weeks before the rupiah devaluation of 30 March 1983 and during the last weeks before the RAPBN (Draft of the State Budget) of 1984/1985 shows that just a small uncertainty in monetary policies can induce big international capital flows.

Such flows can still be managed though there is a free foreign exchange system. The instruments, however, differ from those of a directly controlled regime. If in a directly controlling monetary regime control is exercised through the directives of the Central Bank, in a free exchange system it is done indirectly through the management of the internal and external value of the rupiah and interest rate policy which is continually adjusted to the international environment. The fact that Indonesia's monetary reserves since 1982 have not undergone a continuing decrease indicate that the risks of capital export involved in the free exchange system can be managed through monetary stability adjusted to the prevailing international conditions.

The third indication of the government's will to expand the role of the private sector is the partial deregulation of the banking system of June 1983. The credit ceiling and fixed interest rates established by Bank Indonesia as the chief instruments of banking policies prior to June 1983 have been abolished. Commercial banks are challenged to expand credits up to the limits of their financial resources which in turn very much depend on their success in mobilizing private savings. At least under this regulation, business success of commercial banks is no longer a function of privileges guaranteed by government regulations, but will depend largely on the efficiency of their operation both in mobilizing funds and lending credits. Moreover, this deregulation also means that the selection of customers will depend increasingly on the latter's creditworthiness.

The transition to the free exchange system and the partial deregulation of the banking system also require changes in the money policy of Bank Indonesia. The well functioning of that deregulation will be impeded very much, if Bank Indonesia continues to function as a supplier of liquidity credits on criteria other than efficiency rather than as an institution of which the main function is to manage the liquidity of the whole economy based on criteria



which include inter alia its need for improvement in productivity. And the role of Bank Indonesia as lender of the last resort has also been promoted by introducing new instruments of money policy. The first among these instruments is the certificate of Bank Indonesia to be traded in the money market with the aim of providing commercial banks the opportunity of utilizing excess liquidity or coping with liquidity shortage of short-term nature. The second instrument is the discount facility of which the aim is to make possible for the commercial banks to acquire liquidity from Bank Indonesia against bonds with a discount rate adjusted to liquidity demand. With these new instruments Bank Indonesia can strengthen its open market policy, that is buying bonds to expand or selling them to contract the money supply.

The core of all these changes is the promotion of the efficiency of the banking system and the real sector of the economy. Credit expansion needs no longer be inflationary because it is based on recycling money already in circulation rather than on money creation. But the improvement of the banking system is one side of the medal, while the other side is the improvement of the real sector of the economy. If the room for new undertakings in the production sector continues to be restricted as before, the increase of private investment expected will not materialize.

It is the adjustment in this production sector which is also implied in the demands for debureaucratization or "the taming of the Leviathan" made by various circles. Is it the freeing of the Indonesian economy from enchantments or "Entzauberung der Welt" as termed by Max Weber or the freeing of Prometheus from his chains? *Laissez fair*? It is not that far and it is not that which is meant. But there are various arguments for the expansion of the role of the private sector in economic development, and at the same time also in the social, political and cultural development of Indonesia.

## BLESSING IN DISGUISE

Would the government speak of expanding the role of the private sector if the oil price is still as high as US\$34 per barrel or even higher, the forests of the country are still rich in precious woods, world demand for the main export commodities of Indonesia which moreover are supplied to a great proportion by state enterprises is still growing, or external loans with soft terms are still available in quantities needed? There is an impression that the call of the government on the private sector has for background the difficulties it is facing in development of financing. But this is also an argument, though not a strong one.



Stronger is the constitutional argument contained in the 1945 Constitution, especially the clarification of Article 33 as the product of the legislation of values lived by Indonesian society which among other things consist of recognizing the birth rights of enterprises established by individual initiative and esteem for the entrepreneurial spirit. Certainly this clarification defines among other things that "only enterprises which do not dominate the livelihood of the people are allowed to be in the hand of individuals." The questions in this clarification however are as follows: (1) characteristics of enterprises which dominate or not the livelihood of the people; and (2) the meaning of "in the hands of individuals."

How difficult it is to answer the first question can be illustrated with the following examples:

- a. An enterprise which was small at the time of its establishment carries out expansion due to its success in business so as to employ "many" people whose needs now depend on the success or failure of this enterprise. Must that enterprise be taken away by cooperatives or the state from the hands of individuals? If the answer is affirmative, this means that no enterprise is allowed to be in the hands of individuals because every enterprise has a chance and is surely expected to grow.
- b. Products of an enterprise do not belong to the "basic needs" at the time of their introduction into the market. But in the course of time, that product becomes "basic needs" both as consumer good and intermediate product for many production processes. Is that enterprise allowed to be in the hands of individuals? If the answer is yes, this would mean that no product is allowed to be in the hands of individuals because any product can become part of the basic needs of society.
- c. A specific enterprise produces goods which are basic needs in a certain region such as sago bread in the eastern part of Indonesia, but in other regions they constitute no basic needs or no needs at all. Is that enterprise allowed to be in the hands of individuals?
- d. A specific product constitutes a basic need for a specific group, but not for other groups so that it is facing an "Arrow paradox." How can the political *gremium* decide whether that product is allowed to be in the hands of individuals?
- e. Even a specific product can constitute a basic need only in a specific time such as wheat flour on feast days. Must this product be transferred from individuals to cooperatives or the state?

The answers to those questions cannot be given straightaway. Among other things they depend on the idea "to be in the hands of individuals,"

which seems to be identified with enterprises owned by individuals as reflected in the paper of the Economic Committee of the Preparatory Body of Independence, which *inter alia* states that state ownership does not necessarily mean run by the state. State property can be managed by individuals or co-operatives, and empirically this can be seen in Indonesia's mining and forestry. For that reason, the room of private enterprises within Indonesia's economy also depends largely on the interpretation of the state "control" of production branches involving the basic needs of the people. It could mean total ownership and management; partial ownership and management as in the case of joint ventures with private enterprises. State control could also mean majority ownership or minority ownership with majority vote; control without ownership such as control of rubber plantations owned by individuals. Of no less importance, control can also be carried out without ownership or management, that is control through economic policies such as tax policy, market segmentation as that through Keppres (Presidential Decree) 14-A or through licencing.

The concretization of definitions contained in the 1945 Constitution, Article 33, is ultimately a political decision which among other things is affected by the political atmosphere. But economic variables must also be taken into account in making political decisions because every political decision is conditioned by the availability of economic resources. This seems to be the background of Marx's thesis that social transformation is conditioned by economic transformation from feudal to capitalistic economy. This is also the background of the proliferation of Fabianism (gradual socialism) in England or social democracy in western Europe in general, or Yugoslavia's "Worker's Self-Management" or partial "liberalization" in real socialist economies of today.

One of the economic variables which are most important but often downgraded, if not neglected, in taking political decisions is efficiency. Many kingdoms or states, from thousands of years before Christ up to now, polished their international image by means of prestige projects which ignored efficiency and for that reason are buried between the ruins of those projects. There are many egalitarian programs which are made without reference to efficiency or economic achievement and therefore are recorded in history only because they have caused human sacrifices. But there are also social systems which were willing to learn from failures of this kind and used certain events to enrich the decision making process with economic considerations as done by Tito when in conflict with the Soviet Union, without sacrificing socio-political aims. It is this virtue which seems to be the most actual argument and constitute the background of the plan to expand the role of the private sector during Pelita IV.

Let me pose a few questions of which the answers may be known widely, but



are seldom stated. Why are cooperatives in Indonesia only able to achieve temporary successes? Why do BUMNs (State Owned Companies) slip one by one into the brink of bankruptcy but are never allowed to go bankrupt? Even palm oil plantations on fertile soil of this country with lower labour costs besides, are also inferior compared with their competitors in Malaysia. And why do BUMNs pay lower wages as compared with privately run plantations? Surely not because the government gives bigger privileges to the private sector. And since the answer to this question is known, it is also known that, based on economic criteria, there is no apriori argument to regard the BUMNs as the "favourites" of the Indonesian economic system. Nevertheless, economic arguments are only a part and is not seldom mistaken for a capitalist argument in taking political decisions.

It is not the existence of cooperatives or BUMNs that is questioned here. But it is the management of the trilateral partnership (cooperatives, BUMNs and the private enterprises) in the Indonesian economic system that should be examined, not just to expand the role of the private sector during Pelita IV, but above all to increase the achievement of the Indonesian economic system during Pelita IV and subsequent Pelitas.

## LICENCING AND RENT-SEEKING

What characterizes the management of "the trilateral partnership" in the economic system of Indonesia is licencing, both affirmative and prohibitive. These two forms of licencing has great impact on the achievement of the Indonesian economic system.

Affirmative licencing must certainly be limited in order to have any meaning. There is no such thing as a licence available for everyone. But once given to someone or a specific group, a licence will be treated by its holder as a normal economic good that has the task of maximizing profits. The costs of acquiring the licence will also be kept at a minimal level. Therefore, the holder of a licence will continue to make efforts to close licencing for his potential competitors. In other words, he will hold continual negotiations with the licence giver based on criteria which are much broader than just economic ones. Such negotiations certainly belong to, but constitute only part of, the complex of skill which must be mastered by any entrepreneur. And they give rise to what is called transaction costs, that is costs that have no relevance to achievement. The more licences are required for an economic activity the higher are the transaction costs which must be borne by that activity and consequently also by users of the product or service produced by that activity.



There are also a lot of prohibitive licencing in Indonesia. It may have sectoral scope like access limitation applied to private enterprises in oil industries. But there is also licencing of a regional character like the limitation of establishing new pharmaceutical industries in Java, besides licencing which may have an ethnical character like the limitation of investment credits for non-indigenous entrepreneurs as contained in the Regulation of 22 January 1974. Finally, there is also a prohibition applied to big enterprises in handling certain projects apportioned to "weak entrepreneurs."

Like the affirmative one, prohibitive licencing also causes transaction costs. Those who are not allowed to enter certain business will keep making efforts to gain access, the more so because every regulation contains exceptions. It is these activities which are called rent-seeking activities, that is, activities of individual or group with the purpose of reaping benefit (rent) from existing regulations irrespective of achievement. A coffee exporter can make profits easily by selling the export licence made available to him by coffee export regulations. And such examples are not difficult to multiply.

Because it causes costs that have no relevance to achievement, rent-seeking activities weaken the competitiveness of an economy both in world and domestic markets. And such activities are a common phenomenon which is found in economics with a high degree of regulation, whether it is English, Soviet or Indonesian economy. As long as the Indonesian economy abounds with this activity, the world of its business will abound with rent-seekers or "Oekonomisierer" in the words of Israel Kierzner who has endeavoured to develop a theory on private entrepreneurship. And to that extend will efficiency also be in the lower ranks of criteria of economic decisions, and since the field of activity of rent-making is licencing, the straitening up of licencing and the apparatus empowered to its control is an elementary requirement which must be fulfilled if an increasing private role is really wanted in Indonesia. A strong private role can only be found in a constitutional state where the ruler is laws rather than people.

## STRENGTHENING SOCIAL PEACE

Bureaucracy has become the scapegoat in explaining the inferior achievement of the Indonesian private sector, as if everything would automatically change had the bureaucracy become simpler and more consistent. But accusing solely the bureaucracy is not appropriate. Protection demands submitted by the private sector to restrict competition both in facing foreign competitors and fellow domestic ones show that the private sector is not ready as yet to survive in business on the basis of its entrepreneurial achievements. In other

words, the expansion of the private sector during Pelita IV requires adjustments by that private sector itself.

Among those adjustments is included the improvement of the social and political image of the private sector in Indonesia. The regulation of the Indonesian private sector cannot be separated from the doubts of the state and the public about the social and political responsibility of the private sector. Those doubts have existed since the establishment of this state as expressed in this citation: "Otherwise the direction of production will fall into the hands of individuals in power and common people will be repressed." These doubts still exist today, although due to reflection on our economic system, enterprises in the hands of individuals do no longer mean the repression of the people, but contribute to common welfare. Is it true that through socialization (*Vergesellschaftung*) or nationalization (*Verstaatlichung*) of enterprises, there will no longer be repression? Repression can be understood in various ways. It could mean embezzling the money of cooperatives, embezzling funds for reforestation, compulsion to buy from cooperatives or illegal levies as a condition to get the telephone installed. And these instances are not rare in our country. In other words, repression of our people by enterprises does not depend on their form, whether cooperatives, BUMN's or private enterprises. But it is private enterprises that can easily be blamed in this country. They must improve their image as an historical task not yet accomplished. The growing private role in the economic system of Indonesia will only get broad support if together with the expansion of this role social peace becomes stronger.

Social peace is a *modus vivendi* of social solidarity. This concept is chosen with the exemplification that certain parts of the interests of social elements are not always convergent. Differences of interests cannot always be avoided, but they should be managed to avoid serious disruptions in economic activities. This management should be carried out as much as possible spontaneously by the social partners involved in the activities of the private sector, namely management and labour, and only in overcoming certain difficulties involve the state as a third element in the tripartite institution.

Behind differences of interests between social partners there are common interests which cannot be denied. An enterprise can only stay in business -- and consequently earn money -- if labour productivity rises over times. On the other hand, the improvement of labour productivity requires social tranquility that in turn is a function of income throughout and after working age and the humanization of labour relations. Among the most important variables of social tranquility, and consequently also of social peace, there is the level of wages; social security such as health and accident securities and



pension, the training of labourers; and participation of labourers in managing the activities of the enterprises, both directly in planning the production process and indirectly in management; and, equally important, the income of the enterprise.

Many of these variables have become part of labour relations in Indonesia, though some suffer some inefficiency. For that reason, it is the task of Pelita IV to develop them to become something comprehensive or a social system. If this can be developed, the affirmative attitude toward the expansion of the private sector in Indonesia's development will be socialized. But such an affirmative attitude must be supported by changes in the public sector, including the deregulation of the economy. The partial deregulation of the banking system begun last June, for instance, will not bring forth the results expected, if a comparable deregulation is not carried out in the business world. Furthermore, deregulation will not help much the development of the private sector unless it is supported by an apparatus which is skilled and consequent in implementing regulations which has been made simple on the principle of a constitutional state.

These changes in the public sector will increase competition in the private sector. Access to business will become broader and the selection of business agents will take place on the basis of efficiency. What is called by Harvey Leibenstein as "X-inefficiency," that is inefficiency due to regulation of economy will decrease and entrepreneurs who are not just rent-seekers will shape the private sector of Indonesia. The competitiveness in world markets and within the country to face imports will also increase. And if this process is accompanied by the improvement of the social, political and cultural image, the private sector will become one of the strong elements in "Trilateral Partnership" of Indonesia's economic system, and no longer just a "gap filler" which is activated or frozen depending on the condition of government finance. Nevertheless, the way ahead is long and stoney. One Pelita is not enough, the more so one Pelita which will apparently consists of difficult years like Pelita IV, to put it in order.



# Analysis and Projected Development of Indonesia's Banking Industry

J. PANGLAYKIM

## INTRODUCTION

If we want to see the development of the banking industry today, we cannot put aside the recommendation of Bank Indonesia to the private banks to merge in 1980. This policy of Bank Indonesia was a step towards rationalization.

Since the 1950s banking has always been affiliated to political parties or figures, because at that time political parties or figures were decision makers in the monetary and economic fields. It can be said that there was hardly one political party or figure who did not have any alliance with a bank. The requirements laid down by the technical authority at that time were very easy to meet, so that the total of banks that obtained a licence approached the number of 125.

During that period the growth of the banking industry slowed down, because the business community faced the so-called sellers market. They also did not need the services of banks because the buyers gave cash advance (*voorfinanciering*) without additional interests.

Such a banking situation had led Bank Indonesia to taking rationalization measures by recommending banks to merge. Due to this policy the number of banks classified as sound and rather sound increased. In 1971-1980, the number of private banks decreased from 125 to only 70. This policy also stimulated the growth of the banking sector and succeeded in creating an atmosphere which enabled the private sector to come to the fore with a cleaner image, free from connections with political figures.

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Starting from the situation after the rationalization, we will discuss the development of the banking industry in 1983, when the government adopted the 1 June 1983 Policy. And based on the situation and development in 1983, we will suggest the direction that should be taken in the development of national banking in 1984 and thereafter, namely to develop national banking as growth industry in Pelita IV.

## DEVELOPMENT DURING 1983

In trying to analyze the development of banking industry during 1983, we will discuss the assets and capital reserves, and the credits channeled by every bank. From these figures we will know the position of various kinds of bank in Indonesia. Further, we will see the impact of the 1 June 1983 Policy, which was a step of the government towards the maturation process of national banking. We will also see to what extent the 1 June Policy has affected the development of deposits and extension of credits.

### The Position of Diverse Kinds of Banking

Here we present some data that may give an illustration on the position of diverse kinds of banking in the national business community. This position can be noted from the amount of assets and capital reserves and the credits extended.

Table 1

#### ASSETS, CAPITAL RESERVES AND PROFITS OF BANKS (up to 30 June 1983, in billion rupiah)

	Assets	Capital Reserves	Profits
1. State banks including Bapindo and BTN (7)	16,632	1,103	147.0
2. Foreign Banks including Bank Perdania (11)	1,611	68.4	34.1
3. National private banks (73)	2,499	234.2	39.3

Source: *Berita Perbanas* (Bulletin of National Banking), No. 8 (Oktober 1983).

In Table 1 we will see the composition of assets and capital reserves of diverse kinds of banking.

In terms of assets, capital reserves, and profits, state banks occupy a dominant position, the more so if Bank Indonesia is included. The ratio of the assets of state banks to those of national private ones is approximately 6.66 to 1, whereas the profits of state banks are 3.74 times those of the national private banks. This shows that the productivity level of private banks is higher than of state banks or it may also illustrate that state banks have still to take social responsibility as agent of development. However, with this additional responsibility state banks are still able to show profits which are convincing.

Also in credit extension the position of state banks is still conspicuous. To study the role of each kind of banking in extending credit, we took some data from the *Weekly Report of Bank Indonesia*<sup>1</sup> which is as follows:

Table 2

## CREDIT AMOUNT BY KINDS OF BANK

Kinds of Bank	Amount of credit	%
1. Bank Indonesia	Rp 2.375 milyar	16,24
2. State banks	Rp 9.593 milyar	65,61
3. Rural development banks	RP 390 milyar	2,66
4. National private banks	Rp 1.543 milyar	10,55
5. Foreign banks	Rp 719 milyar	4,91
	Rp 14.620 milyar	100,00

The total Credit extension by the state banks, Bank Indonesia and the regional development banks amounted to 84.53 per cent of the whole credit extension, so that one might say that the position of the government's sector is quite dominant compared with national private banks. National private banks and foreign ones only extend respectively 10.55 per cent and 4.91 per cent of the whole credit. If the off-shore operations of state bank agencies are taken into account, the share of state banks in the credit extension will be bigger.

Pursuant to the dominant position of state banks, the pattern of credit extension also depicts an increase of the government sector, state companies and projects financed by the government.

Of the total sum of credits until the first week of October 1983 which amounted to Rp 14,620 billion, the composition of the total credit extended by the state banks can be seen in Table 3.

<sup>1</sup>*Weekly Report of Bank Indonesia*, No. 1280, 17 November 1983. The figures comprise those up to the first week of October 1983.



Table 3

## CREDIT EXTENSION BY ECONOMIC ACTIVITIES

	Sum	%
1. Agricultural sector	Rp 1,397 billion	9.56
2. Mining sector	Rp 1,017 billion	6.96
3. Industrial sector	Rp 5,640 billion <sup>a</sup>	38.58
4. Trade sector	Rp 4,635 billion <sup>b</sup>	31.70
5. Services sector	Rp 1,268 billion	8.67
6. Other sectors	Rp 663 billion	4.53
Total	Rp 14,620 billion	100.00

<sup>a</sup>Including Pertamina's debt to the government in the framework of paying its foreign debt.

<sup>b</sup>Including the provision of food and hotel.

## Deposit Development

The 1 June 1983 Policy which among other things abolished the ceiling of credit extension to all banks, allows the state banks to determine the interest rates of their respective time deposits (for national private banks the regulation on the interest rates of time deposits has no longer been in force since a long time) has brought about a development as shown in Table 4.

In Table 4, we can see an increase of the sum of deposits of Rp 669.9 billion or 73 per cent, namely from Rp 911.8 billion in January 1983 to Rp 1,581.7 billion in the fourth week of September 1983. Viewed from their time, time deposits of 24 months have decreased, while those of 12 months have increased. The most striking increase of the sum of deposits has been that of 3-months deposits, which have increased from Rp 8.1 billion in May 1983 to Rp 297.7 billion in September 1983.

At first it was estimated that 24 months deposits declined because some of the customers were afraid to deposit their money for a long period of time because of the possibility of the adoption of another new monetary policy. But it has turned out that they had transferred the 24 months deposits to those with a shorter period of time, 12 or 6 months. Whereas the increase of 3 months deposits was due to the fact that funds were or were not yet used while business activities were slowing down. An income from interests ranging between 16 per cent to 18 per cent a year from deposits could be regarded as reasonable in a situation where business was slumping.

Table 4

TIME DEPOSITS OF STATE BANKS  
(Summary)

At the end of	24 months	18 months	12 months	9 months	6 months	3 months and less	Total
May	835.6	-	41.2	-	26.9	3.1	911.3
June	763.2	-	111.9	-	119.3	129.3	1,124.0
July	726.4	-	217.9	-	143.8	200.0	1,287.1
August	684.1	0.2	352.7	0.1	200.3	262.7	1,500.1
September-III	661.1	0.6	408.9	0.1	213.5	290.5	1,574.7
September-IV	655.3	0.7	417.0	0.1	210.4	297.7	1,581.7

Source: *Weekly Report of Bank Indonesia*, No. 1280 (17 November 1983), pp. 20, 23, 24, 25, 26 and 27.

According to observation, those who deposits their money for a period of 3 and 6 months are from business circles whereas those who deposits their funds for a longer period of time (12 and 24 months) usually comprise non-business people such as professionals and civil servants. By depositing their funds for a shorter period of time, business people will have an option in case they unexpectedly need money in an improving business situation. In the years to come, it is estimated that many medium and small entrepreneurs will need additional funds from outside the banking sector. The medium and small entrepreneurs will do so because it will be easier for them to get those funds from outside the banking sector (the extension of credits is calculated on the basis of personal relationship) and to avoid taxes. If they want to get loans from banks they will have to show their tax-payer's number which most of them do not as yet have. Some time ago, their needs were channeled by banks to market banks, but some time in the future market banks will also require the taxpayer's number from their customers. Should this be the case, it can be expected that the market outside the banking sector would be liven up.

Table 5 shows the development of time deposits at private foreign exchange and non-foreign exchange and state banks. Apparently deposits at the former have also increased although a quite striking difference can be noted. The sum of time deposits at private foreign exchange banks in September 1983 amounted to Rp531.3 billion and at private non-foreign exchange banks Rp213 billion. And if we compare it with the sum total of time deposits of foreign banks, it turns out that deposits of non-foreign exchange private banks were less. Foreign banks have been able to collect deposits from their customers amounting to Rp507 billion up to September 1983, although the deposit interest rates they offer are usually lower than those of foreign exchange and

non-foreign exchange private banks. This may have something to do with the aspect of trust or feeling. The public are apparently inclined to deposit their money in state banks, then in foreign exchange private banks, foreign banks, non-foreign exchange private banks and finally in development banks (among those various kinds of banks, non-foreign exchange private banks offer the highest interest rates).

Table 5

TIME DEPOSITS OF BANKS IN INDONESIA  
(Summary, in billion rupiah)

Year	National Foreign Ex- change Banks	State Banks	Private Foreign Ex- change Bank	Private Non-foreign Exchange Bank	Foreign Exchange Banks	Ex Devel- opment Bank	Clearing Parti- cipants
1983							
<i>Month</i>							
May	1,546	(911.8)	(634.2)	146	520	56	2,268
June	1,788	(1,124.0)	(664.0)	168	486	59	2,501
July	1,946	(1,287.1)	(658.9)	181	503	59	2,689
August	2,029	(1,500.0)	(528.9)	193	501	60	2,783
September	2,113	(1,581.7)	(531.3)	213	507	60	2,893
October	2,456	(n.a.)	(n.a.)	219	550	62	3,287

Source: *Weekly Report of Bank Indonesia*, No. 1280 (17 November 1983), pp. 24 and 26.

### Development of Credit Extension

Credit extension, after the abolition of its ceiling, has apparently not increased strikingly. The highest increase occurred some time between the end of December 1982 and March 1983, namely at 5.2 per cent, but after June up to October 1983, its increase only ranged between 0.1 per cent to 2.4 per cent (see Table 6).

Former Central Bank Governor, Mr. Rahmat Saleh, said in his address to bankers, that the credit extension ceiling would not increase much. At that time banks clamored for the loosening of the ceiling. After the credit ceiling was abolished by the 1 June 1983 Policy, it turned out that there has been no excessive increase of credit demands. This may be due to the increase of interest rates a result of the rising cost of money of banks including those of the state or government. State banks that previously imposed an annual interest rate of 12 per cent, had to raise the interest rate. Another cause may be that business was still slack and business people tended to deposit their idle money in the form of short term time deposits of 3-6 months. If this was the



case, it can be said that the 1 June 1983 Policy has succeeded in curbing the credit level at a natural ceiling, or perhaps bankers may have reached a mature level, namely they -- have been more careful in extending credits. Today banks have quite high liquidity as is reflected in the level of the inter-bank interest rate which has declined to around 14 per cent, whereas in the months of April and June 1983 it once reached 24 per cent.

Table 6

CREDIT EXTENSION DEVELOPMENT OF NATIONAL BANKS  
(in billion rupiah)

	1982			1983			
	December	March	June	July	August	Sept. 1V	Oct. 1
1. Bank Indonesia (direct loans) (2)	2,771	2,388	2,293	2,307	2,287	2,362	2,375
2. State Banks (4)	8,031	8,854	9,062	9,195	9,374	9,549	9,593
3. National Private Banks (5)	1,197	1,354	1,403	1,391	1,483	1,532	1,543
4. Rural Develop- ment Bank	357	372	381	382	387	389	390
5. Foreign Banks	666	737	661	694	728	776	719
Total	13,022	13,705	13,800	13,969	14,259	14,608	14,620
Increase		5.2%	0.7%	1.2%	2.1%	2.4%	0.1%

Source: *Weekly Report of Bank Indonesia*, No. 1280 (17 November 1983).

## TOWARDS THE GROWTH OF BANKING INDUSTRY?

After analyzing the banking industry from diverse angles, the following is a personal view on the possibilities of growth of the banking industry sector in the years to come. This is not a soothsayer's view, but rather an estimate based on some considerations expected to boost the banking industry towards the creation of means for faster development. In my view the creation of those means would be more real if other business and economic sectors at the national and international level would also undergo changes. Consequently, national banking industry would be faster directed towards the creation of those means so as to become a strong growth industry.

### The 1 June 1983 Policy

The banking industry observers and other business actors often see the past as a time of consolidation and the creation of an atmosphere where trust in the banking industry can recover. It is not surprising that in the consolidation process the banking policies which constitute a guidance are often considered just as a constraint. This may be due to the fact that the dynamics of the development of the banking industry has been too fast in comparison with its policy. Indeed it cannot be denied that the policy which is adopted by the authority concerned will always be considered as "too late" compared with the reality that is evolving in the business arena. With that perception, the banking industry accepted the 1 June 1983 Policy as a step to refresh the view of the government (in this case Bank Indonesia) with regard to national banking industry. The government (Bank Indonesia) has apparently realized that the national banking is on the way to maturity.

The first measure of the 1 June 1983 Policy is to give more room for activities such as extending licences to open branch offices, rescinding fixed interest rates, abolishing the credit ceiling. This may perhaps be regarded as the initial steps of directing the banking industry towards growth industry. But in examining the development of banking industry we should not fix our view on the government's policy only, but it may be useful if we take into account the forces in other business arenas. Aside from that one should also consider the forces that may arise in the process of boosting up the banking industry towards a more sophisticated level.

Some time ago the private sector made a request to the government to form a kind of Danareksa Limited to be managed by the private sector (bankers and other business prominent figures). To the request, the government has not given a positive answer as yet (it has been neither rejected nor accepted). It may be due to the absence of regulations of the authority in monetary field. In connection with the 1 June 1983 Policy and the promotion of the banking sector toward growth industry the possibility of establishing such a limited company (PT) should be reconsidered in order to establish closer cooperation between the two business sectors, namely the government and the private sector. Or perhaps one should also consider whether a similar Limited Company which already exists, namely PT Sarana Bersama Pembiayaan Indonesia (SBPI), can be exploited.

As is known, state or government banks have forums, for cooperation, for example, Perbanas for private banks and the Banker's Club for bankers. Cooperation between state and private banks (foreign exchange and non-foreign exchange) is established in the form of a forum of shareholders of ASEAN Finance Corporation (AFC) which is called "PT Sarana Bersama



Pembiayaan Indonesia." State and private banks respectively own 50 per cent shares.

### **Export and Banking Strategy**

Developing countries, including ASEAN and Indonesia in particular, are today making efforts to find alternatives of promoting exports and foreign exchange earnings. Indonesia has decided on her strategy, i.e. non-oil export strategy as one of the important alternatives aside from that of oil and LNG. If we look deeper into the matter, the greatest potential of attaining the target fixed by Pelita IV is in fact the promotion of the export of industrial and manufacture products and industrial raw materials. From the experience of other countries it can be inferred that the industrial and manufacture products may be expected to become alternatives aside from other products such as shrimps, plywood, and oil palm.

When the strategy has been decided, namely that of export, and all forces have been unified and directed towards the implementation of that strategy, various scenarios may be expected to emerge.

The existing manufacture industry has to be reorganized and reoriented towards export. At present, all joint ventures with Japanese partners, for example, are basically directed toward taking advantage of domestic markets and consumers. They have to reorganize although it has to be admitted that it would not be easy.

Aside from the existing industries, hundreds of new industries oriented towards export are expected to arise either in the form of joint ventures or national enterprises (Domestic Investment). Each of those units of production should be capable of creating products which are competitive in the international markets in terms of price, quality and marketing means. To this end several factors should be taken into account and these are among others: (a) Assortment of manufacture products; (b) Product assortment that has to be accompanied by service assortment.

### *Assortment of Manufacture Products*

If the establishment of hundreds of manufacture companies has been realized, rubber, petrochemical, and aluminium products, for example, will broaden the range of Indonesia's manufacture products. And since those products are oriented toward export, their price and quality are expected to be and should be competitive in international markets and could meet the consumer's demand. The assortment of manufacture products would stimulate other institutions to make changes because the marketing of those products would be



very different from the export or marketing of agricultural products in the form of raw materials. Also the consumers would no longer be institutional consumers (factories, for example) but millions of final consumers throughout the world. The channelling of those products should also be done through what is known as the general trading firm concept.

Looking at the markets around us, we will see that developing countries will make continuous efforts to introduce their industrial products into the markets of industrialized countries including Japan. There will be keen competition. What should Indonesia do, sell them directly? Are its trading institutions indeed capable of having direct access to the markets of industrialized countries? Or should Indonesia establish cooperation with foreign partners and/or utilize the general trading firms (Sogo Shosha, for example) with their international network? If Indonesia uses the general trading firms or Sogo Shosha, would it again be paralyzed and depend on those trading firms? Or would it be possible for Indonesia to establish cooperation with them for a time? To answer those questions one needs an indepth study. A trading group that already has an international network, such as Liem Soei Liong Group with Hagemeyer as their trading firm, may be regarded as a concrete effort toward preparing for the implementation of the export strategy.

#### *Product Assortment Has to be Accompanied by Service Assortment*

At the first stage of the product assortment development, hundreds of manufacturing companies will take the form of companies with domestic capital (PMDN) or national companies that have made adjustments. Accordingly, banks will be approached by the initiators of those industries. But the problems is, will the banking sector already be capable of giving services to them? Will the banking sector be able to act as provisional pioneers in taking equities as this is not as yet allowed? Will this situation change during the development? This change is a very important aspect in making the export strategy successful although, it must be acknowledged, it would be very difficult to apply. If the taking of equities will still not be allowed, part of the business activities may shift to the foreign banking sector. But provided that it be allowed, would the banks with a pattern of funds which are rather short term in nature be capable of financing the long-term equities? Would they be able to mobilize capital directly from the public by issuing bonds or obligations? State banks and private foreign exchange banks may be more successful in mobilizing funds from the public than private non-foreign exchange ones. All of these should be studied deeper.

In connection with the implementation of the export strategy in the years to come our business community will also needs more varied services from the national banking sector. Banks are not only regarded from the viewpoint of

granting credits, but they also desire that the credit be improved in quality and varied, such as in the form of floating rate notes (FRN), syndicated loans commercial papers, promisory notes.

Other banking services such as market information, advice in determining the financing of exports or factories, will be greatly needed so that bank officials as well, in turn, should show a more sophisticated development. Professional managers may also have to be assisted by professionals who know about energy, marketing and the like.

It can be briefly pointed out that the needs of the business community will be varied, hence the banks should also prepare in the best possible manner in order to be able to meet the demands of their customers. Traditional activities such as extending credits will still be performed but they should be accompanied by other services, because if national private banks do not succeed in providing those services, their role will certainly be taken over by foreign banks. Hence, the banking sector should from now on prepare a network of endeavours, information, and offices at the international level. State banks such as BNI 1946 and Bank Eksim (Export and Import Bank), for example, have expanded by creating a network of branch offices in the United States of America (officially opened on 5 December 1983). Those efforts of expansion should be intensified. National private banks, particularly foreign exchange banks, have not as yet been allowed to expand their network into the international market. It may be advisable to make an indepth study on the possibilities of allowing foreign exchange private banks to expand their network at the international level.

Consequently, in the years to come, the policies on: (a) the criteria of foreign exchange banks; (b) merger; (c) opening of branch offices in the international market; (d) equity finance, should be reconsidered. Some points will have to be changed, some others will have to be loosened, and some to be retained. In brief, these policies may lead to the successful implementation of the export strategy of non-oil and gas products. The difference between investment banks and commercial banks, for example, will perhaps be abolished (this aspect is very difficult to solve and will need a long time). Or perhaps efforts to make banks go public will be considered? In the framework of creating global banking, should the requirements to become a foreign exchange bank be tightened with technical qualifications or should the less pragmatic requirements be alleviated? Will the door to the banking sector remain closed for the groups of big enterprises, and must they spend, for example, Rp23 million to buy a bank? If the way to this sector has been closed, does not it mean that those who are already inside will have a kind of monopolistic position? See, for example, the price of merger, which is near Rp3.5 billion, for a bank with one branch office. Those who are already inside may object to "opening the



door'' again, because once the door has been opened the market price of bank mergers will go down.

Various arguments on the pros and cons of opening the door to the banking sector have been put forward. Bank Indonesia is apparently inclined not to extend licenses for opening new banks. Allowing international banks to open branch offices may even be more difficult. Various prerequisites have to be considered which will serve as criteria for the foreign exchange banks. One of the most important criteria is to set the structure of funds since this is connected with the possibility of equity finance. Other prerequisites may be in the form of capital level, experts, the banking business itself, and the implementation of the export strategy.

## CONCLUSION

After examining the figures of assets and capital, deposits, credit extension, national and international network, profits and the like, apparently state banks still hold a dominant position. Meanwhile private banks (foreign exchange and non-foreign exchange) are still lagging far behind. And, considering the economic structure of Indonesia, it can be concluded that state banks will maintain their dominant position while national private banks are considered as essential complements. Between the two banking sectors cooperation has been established in the framework of PT Sarana Bersama Pembiayaan Indonesia (PT SBPI) of which 50 per cent shares are owned respectively by the state and the private banking sector.

On the other hand, the role of foreign banks (considering the figures of the *Weekly Report of Bank Indonesia*) operating in Jakarta, may be said as still insignificant, but in view of the activities of their agencies' and their offshore endeavours it can be said that the funds they have been channeling are quite substantial.

The monetary policy which was adopted on June 1, 1983 is seen as a first step toward the maturation of national banking. The adoption of the export strategy will create an atmosphere and forces that will push national banks to a more sophisticated development. But this development will certainly depend to a great extent on seriousness, coordination and the right policy to make the implementation of the export strategy successful. If development is carried out properly the forces will most likely boost national banking towards growth industry in Pelita IV. But we are still facing a variety of questions of which the answers call for a more indepth and thorough study. Changes are expected to occur, but the problem lies in the speed of those changes. The private sector may have time horizons which are different from one another especially from those of the policy makers.



# **Expectations and Prospect of Development in the Socio-Cultural Field during Pelita IV**

A. Sudiharto DJIWANDONO

## **SOCIO-CULTURAL GOAL**

National development which started in 1969 and on 1 April 1984 entered the stage of the Pelita IV (Fourth Five-Year Development Plan) is not just economic development, though so far the development of this field has been given high priority. Development which is centered just on economic development ("econo-mo-centrism") has been abandoned due to growing awareness about the main or essential meaning and aim of development efforts, which is none other but man himself. What is called economic goal in development, on another degree of analysis, is not entirely economic. The economic goal of increasing income and productivity, for instance, which in its turn constitutes a means for attaining the goal in the form of the possibility to achieve a better and fuller life for the members of society. In other words, each goal of development has a socio-cultural character.<sup>1</sup>

There has been a shift from development which has the character of "econo-mo-centrism" toward development which has the character of "homino-centrism," where man becomes its center. It is socio-cultural factors which determine and constitute at the same time the ultimate result. Development should always be geared to increase the welfare of man and improve the quality of life, which cannot be measured just with economic measures. Per capita income, available infrastructure, health facilities, number of available hospitals, or the ratio between doctors and inhabitants, and others, all those things constitute indicators of the degree of wellbeing and quality of life.

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<sup>1</sup>Janusz Ziolkowski, "Cultural Dimensions of Development," *Cultures*, vol. vi, no. 1(1979), pp. 17-18.

However, those measures alone are not yet sufficient because quality is a matter of interpretation, perception and ultimately a matter of evaluation. In principle the demand for a better quality of life is a political demand or rather an ethical one.<sup>2</sup>

Indonesia's national development which is currently going on is also development that centers on man, in this case the Indonesian man.

GBHN (Broad Outlines of the State Policy), Chapter III, General Pattern of Long-term Development, sub B., Direction of Long-term Development, clearly states, that "National development is carried out in the framework of a total development of the Indonesian man and the development of the whole Indonesian Society." Further it is stated: "This means that development is not just the pursuit of material gains such as food, clothes, housing, health, etc. or non-material satisfaction such as education, security, freedom of expressing responsible opinion, justice etc., but a harmony, concord and balance between the two; that development shall extend to the whole country; that it is not just meant to a particular group or part of society, but for the whole society and must be felt by the whole people as an improvement of their standard of living with social justice which is the aim and ideal of our independence. The Indonesian nation desires a harmonious relationship between man and his God, between fellowmen and with their physical environment, a harmonious relationship among nations and also a harmony between the ideal of life in this world and the achievement of happiness in the world to come, because the harmonious life of man and society constitutes the ultimate goal of national development; in brief, a society which is developed, just and prosperous, and based on Pancasila."

That citation of GBHN clearly shows that the long-term aim of our national development is no other but the Indonesian man himself and the whole Indonesian society. By means of national development efforts which are carried out in stages we want to create a society of the Indonesian nation which is united, prosperous and with social justice where each of its members lives in external and internal wellbeing.

"Whole man" is a man who lives in welfare externally as well as internally in a harmonious balance between those two aspects. Internally he is a human being who is conscious of values, examines values and looks for values.<sup>3</sup>

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<sup>2</sup>Peter Atteslander, "Reflections on the 'Quality of Life' as a Function of Social Structures and Social Change -- Sociological Perceptions," *Universitas*, vol. xxii, no. 1(1980), p. 63.

<sup>3</sup>Daed Joesoef, "Pendidikan Nasional Membentuk Manusia Seutuhnya," *Sinar Harapan*, 24 January 1984.



Therefore it is clear that in principle the goal of our national development is a socio-cultural one. Economic development which thus far has been given high priority in our national development is not the ultimate goal of that national development. To some extent, the economic field must have high priority because without improvement of this field the long-term goal mentioned will not be attained. What is required is that while giving high priority to the economic field we should not neglect non-economic fields but should develop and gear them to positive development. Such measures are important because economic development of necessity has its impact on non-economic fields, which might develop in an undesired direction when they are not properly dealt with from the beginning.

### PANCASILA, A NATIONAL CULTURAL CONCEPT

In its broad meaning, culture is interpreted as the whole of thoughts, work and results of human work which are not based on his instinct and therefore can only be created by man after a process of learning.<sup>4</sup>

The Mexico City Declaration on Cultural Policies of 1982 states that today "Culture can be said the whole set of qualities of the soul, matter, intelligence and feeling, which shows the characteristics of a society or social group. It does not only include art and literature, but also life styles, human rights, values system, traditions and beliefs."<sup>5</sup>

In any case, in the concept of culture a number of things can be identified, namely spiritual aspects, thoughts and human feeling, work or activity of man and its results. Culture always shows the character and special qualities of a nation, society or social group. Man can only bring about culture with all its aspects after a process of learning, because that "potential" is not rooted in his instinct.

Considering those aspects of culture, Prof. Koentjaraningrat believes that culture has at least three forms, which are: (a) culture as a complex of ideas, thoughts, values, norms, rules, and the like; (b) culture as a complex of patterned behaviour of man in society; and (c) culture as things made by man.<sup>6</sup>

National development which in the long-term is directed to the total development of man and the development of the whole society means that

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<sup>4</sup>Koentjaraningrat, *Bunga Rampai Kebudayaan, Mentalitet dan Pembangunan* (Jakarta: Gramedia, 1974), p. 11.

<sup>5</sup>*Cultures*, vol. ix, no. 1(1983), p. 15.

<sup>6</sup>Koentjaraningrat, *Bunga Rampai Kebudayaan*, p. 15.

through development efforts and activities the forms of our national culture must increasingly be realized, made more real and form the character and special qualities of the Indonesian man and nation.

We already have Pancasila as the philosophical basis of the state and view of life of the nation which constitutes a complex of fundamental ideas and values taken from the history of the nation throughout the centuries. Those values must become the basis, norm and direction of every activity of the Indonesian man in his personal life as well as in his relationship with the state and in his social life in general, and must be able to generate works which radiate those values. In other words, Pancasila is our cultural concept which we need and must maintain and develop further.

Efforts to maintain and develop that cultural concept so as to be more deeply planted, realized and understood by every one with a view to implementing it is a continuous process of development and learning. From this standpoint national development constitutes the way to cultivate, to develop and to practice Pancasila culture with a view to achieving its long-term goal, that is the total development of the Indonesian man and the development of the whole Indonesian society.

It is understandable that in 1983 the MPR (People's Consultative Assembly) enacting GBHN stressed that we regard national development as the implementation of Pancasila. In this connection, President Soeharto said in his address on new year's eve 1983, that the emphasis of our struggle has been progressing, from securing to implementing Pancasila. Although -- according to the President -- of course in that stage of implementing Pancasila we shall not slacken our watchfulness against latent dangers from extreme forces which from the beginning have not been in accordance with Pancasila.

As is said above, because the goal of our national development is the total development of the Indonesian man and the development of the whole Indonesian society, through this development it must be possible to achieve a situation where Pancasila culture is socialized or to achieve a Pancasila society. To build Pancasila society is to build and develop culture, Pancasila culture. And the ultimate goal of the whole cultural development is to create a humane society. The Declaration issued by the Conference of Ministers of Culture of Asia in Yogyakarta on 19 December 1973 among other things states: "To bring about a humane society is the ultimate objective of the whole cultural development."<sup>7</sup> Thus, to build Pancasila society is in principle to build a society which enables all and each member to live properly as a human being, to

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<sup>7</sup>Kirdi Dipoyudo, *Pancasila, Arti dan Pelaksanaannya* (Jakarta: CSIS, 1979), p. 75.



build and develop himself and to achieve the fullest and completest possible life in accordance with his human dignity.

National development as the implementation of Pancasila concretely means to build, develop and realize Pancasila political life, Pancasila economic order, Pancasila social and cultural life, Pancasila legal system, Pancasila educational system, in brief a development covering all aspects of life which are inspired by and based on Pancasila values. All fields must be built and developed on the basis of Pancasila, the philosophical basis of the state, the view of life and morals of the nation. This is a consequence which cannot and should not be avoided because we have accepted Pancasila as the philosophical basis of the state. Pancasila values must radiate from each aspect of the life of the state and society as realization of the implementation of Pancasila.

This obviously constitutes a tremendous task and takes time, because what is built is in principle a man, in this case the Indonesian man. The situation will become increasingly critical when state officials, leaders of society and leaders in general do not as yet manifest "Pancasila man" as it should.

Our society which according to experts still has a fairly high content of paternalism, places leaders both formal and informal as "examples" of society. Society in general will always note and emulate what is said and done by its leaders.

The ideal is of course that Pancasila values are increasingly understood, lived and practiced by every Indonesian man. Everyone understands rationally and accepts emotionally these values in order to implement them in their daily lives. In the language of education, the cognitive, effective and psychomotoric aspects must be developed to cover what we call the living and practice of Pancasila. Against practices which are at variance with Pancasila values, be they a situation or action or policy, one's reaction will not only be moved by the functioning of sound reason but also by his feeling involved. A situation, which is judged improper by sound reason, also touches the feeling. This holds for any aspect of our social and political life, injustice, corruption, discrimination, poverty and the likes.

From this angle we see how important the Decree of the People's Consultative Assembly No. II/MPR/1978 known as P-4 (Pedoman Penghayatan dan Pengamalan Pancasila -- The Guide to the Living and the Practice of Pancasila) is which has been issued with a view to socialize the values contained in Pancasila as part of efforts to bring about Pancasila society. Pancasila as the cultural concept of the nation containing noble fundamental values can only be implemented through a process of learning, in which one increasingly

knows and understands and lives those values. And someone who truly lives a value will of course apply or implement it in the practice of his daily life.

However, it should also be realized that in the political and social life in general, the implementation of Pancasila will very much be determined by their deduction into every legislative and other regulations. Any legal regulation of whatever level must be rooted on Pancasila values and constitute their expression.

That is the chief reason for developing a legal system in Indonesia which is a state based on law. It is a continuous effort toward the perfection of our national legal system, which can briefly be called Pancasila legal system.

That argumentation also shows the importance of education in general in the framework of the planting, cultivation and development of values toward their implementation. As is argued above, Pancasila as the nation's cultural concept constitutes a complex of basic ideas and values, which can only be acquired after a process of learning, in which one increasingly realizes, understands and lives those values, so that his personality is really "imbued" by those values and radiates them in his attitude and actions.

This does of course not mean that this is the only meaning and function of education. Because education, especially formal education, must be able to enlighten the life of the nation, so that academical or intellectual education is very important. To develop man totally of course also implies the concept of an intellectually developed man, who has the ability to master and develop science and technology with a view to furthering the welfare of the nation and mankind in general.

For that reason education occupies a very strategic position in national development besides the economic and other fields. Our national educational system which is none other than Pancasila educational system has the heavy and lofty task of developing Indonesian men who realize and accept with their whole personality the noble values of Pancasila, who are intelligent and master matter thanks to their mastery of science and technology. At least that is what we expect from our national educational system, though at the end of the Pelita III there were still doubts in society about some policies implemented in the framework of the development of the national education's system.

Beside the system of formal education, that of non-formal or informal education has an important role to play, especially in connection with the process of realizing, understanding and developing values. Among other things this can be done by efforts to socialize P-4 as carried out so far in the form of P-4 upgrading courses which are extended increasingly from the national level to



that of the regions. In this context it should be noted that the success or effectiveness of these efforts will of course be determined by various factors such as the methods used, the teacher and participants and others. As is the case with the process of learning within formal education, teachers, pupils, infrastructure, means and environment are factors which determine the success of that process.

From a more specific angle, because what will be planted in this process are values which are expected to become guides for attitude and behaviour, models and exemplary conduct occupy an important position and are crucial factors.

Aside from upgrading, the socializational process goes through the channels of family, social intercourses and practices of the life of the state and society in general. Apparently that is one of the considerations of the MPR stating in its Decree No. II of 1978 on P-4 that P-4 is intended as a directive and rule of conduct for the social and political life of every Indonesian citizen; that every Indonesian citizen, every state official and every state and social institution, both at the central level and in the regions, need to make serious and continuous efforts to live and implement the values contained in Pancasila. This process will be a long one and will take time, but at least it has begun. What is likely to be done is continuous efforts to improve efficiency and efficacy with a view to helping achieve the long-term goal of national development.

#### PELITA IV: PRECONDITION PERIOD

Pelita IV which was embarked upon on 1 April 1984 is a very important period in national development. In the stage of national development which was started with the Pelita I of 1969, it was hoped that the coming Pelita IV, or the last five-year period of the twentieth century, will constitute the take-off stage of national development. This means that Pelita IV and V constitute the precondition period for the take-off, in which all efforts should be made and geared to strengthen the framework needed for the take-off. In the period of Pelita IV we are strengthening that framework, while the period of Pelita V will be the period of its consolidation.

The pre-condition period is one of transition, that is transition from traditional to modern society. Old patterns are not yet totally abandoned, but on the other hand new modern ones have not yet found their stable form.

In the economic field it appears among other things that the process of industrialization has started applying modern production methods, but the role of the agricultural sector in the economy is still quite significant. During Pelita

IV, the emphasis of development continues to be on the agricultural sector, while the industrial sector is developed and upgraded toward industries capable of producing machinery, both heavy and light industries. Growth in this industrial and other sectors outside of the agricultural sector will be accelerated during the Pelita IV than that of the agricultural sector with a view to achieving a well-balanced economic structure, which constitutes one of the goals to be achieved in economic development. Efforts toward that goal are projected into growth rate of 9.5 per cent per year for the industrial and 3 per cent for the agricultural sector. On the whole the rate of economic growth during the Pelita IV is estimated at 5 per cent. Should the growth rate of the population during Pelita IV be reduced to about 2 per cent as is estimated, during Pelita IV will be achieved a real increase in the per capita income of 3 per cent.

Of no less importance in the context of strengthening the framework for the take-off is the continuing and increasing of development in non-economic fields, both socio-political and socio-cultural. In an indirect way this was mentioned by President Soeharto in his state address of 16 August 1983, where among other things is said that to strengthen the basis for take-off, during the Pelita IV it must be possible to create an "overall Pancasila atmosphere."

This confirmation can be interpreted that during the period of the Pelita IV and V, Pancasila values and norms must be increasingly implemented in all aspects of the life of the state and society in general. A development which has reached the take-off stage can generally be understood to mean that in society conditions have been established needed to enable the process of development to go on normally, that is, a development supported by forces and mechanism in that society itself. The supporting factors meant are not just economic but also political, social, cultural, defence and security factors.

That is why during the period of Pelita IV and V efforts must be made in order to complete and consolidate the results of development in the political, social, cultural, defence and security and other fields which are non-economic achieved during the three previous Pelitas, including steps to correct and perfect whenever needed. The provision in the GBHN which establishes Pancasila as the sole principle for socio-political forces in Indonesia is one of the steps deemed necessary by the MPR to complete the reform of political life of which the process was started before the Pelita. During the Pelita IV, this process is expected to continue and become increasingly stable, among other things due to ever wider acceptance of the Pancasila sole principle by social organizations besides the three existing socio-political forces. That way the political condition is expected to become more stable as one of the important conditions for the take-off, although it needs also be said that there is in-



terdependence between the political and the economic, social and cultural fields. Moreover, stability in the political field is not only determined by socio-political forces and social organizations, but by the whole structure and mechanism of national politics, including state institutions with their apparatus. This means that political development must be implemented broadly and profoundly, involving ideal aspects such as values and ideology as well as institutionalization with its rules of the game with a view to realizing Pancasila political life.

One of the important marks of Pelita IV as a precondition period for the take-off is the main position given to social justice in order to improve the living standard, education and welfare of the whole people in a just and even way. In other words, the problem of spreading development and its results to implement social justice will be dealt with more seriously than during the previous periods. In this context it can be noted that during the Pelita III eight equitable distribution channels were established, so that during the Pelita IV its implementation can be expected to intensify, both in terms of the budget made available and in terms of its integrated tackling so as to make it more effective.

In addition to intensifying the implementation of the eight channels of equitable distribution, what needs special attention in order to implement social justice are serious and consequent measures against practices which are clearly at variance with social justice, particularly acts of corruption which are still observed everywhere. This is closely related to the intention of the Head of State to establish a clean and authoritative government by improving the effectiveness of the state apparatus both civil and military, as stated in his state address of 16 August 1983.

Regarding the intensified implementation of the eight equitable distribution channels during the period of Pelita IV, steps need to be taken to expand the role of the private sector in various fields, not only in the economic but also in non-economic fields such as education, health, employment and others. In this context, the equitable distribution of business opportunities will play an important role due to its ties to the other equitable distribution channels, such as the equalization of income, employment, participation in development, education and health. Expanding the role of the private sectors will also be important for mobilizing domestic resources which during the take-off stage must become the main supporting factor in the process of development. The set of steps which have been taken and will be taken in the economic field with a view to strengthening the framework such as increasing the export of non-oil commodities, tourism, reform of the taxation system, encouraging and mobilizing savings by the people and credit renewal policies, all those steps require the

expansion of the private role to be successful. The more so when one recalls that during the period of Pelita IV manpower will be a quite heavy problem which we shall be facing so that expanding the role of the private sector constitutes one of the opportunities for job seekers as realization of efforts to provide equitable employment opportunities.

With regard to the socio-cultural field, without ignoring other elements, education is a very important problem which must be dealt with in a serious way during the pre-condition period. It is even no exaggeration to say that the field of education occupies a key position within efforts of national development. Basic ideas of belief in God, just and civilized humanity, Indonesian unity, democracy and social justice, that is, basic ideals which are contained in the Preamble of the 1945 Constitution can in principle only be implemented when efforts to educate people are successful. But we cannot develop education in an economic situation which is chaotic, in disorder and of low level. Thus there is a close relationship between the goal of promoting common welfare and that of educating people as stipulated in the fourth paragraph of the Preamble to the 1945 Constitution. Efforts to educate people will only be successful when there is an adequate level of welfare, but efforts to increase that common welfare will only be achieved and maintained with a high level of education.

In this context, the strategy of national development implemented since 1969 through Pelita stages can be accounted for, that is the strategy of giving priority to economic development without neglecting the development of other fields, including that of education. During Pelita IV as a pre-condition period for the take-off stage the time has come to accelerate the development of non-economic fields without reducing the rate of economic development, so that the basis of which the first stone was laid fifteen years ago on 1 April 1969 becomes increasingly strong, and during Pelita IV we are really taking off. This means that in society conditions have been created which enable the process of further development to take place in a normal and autonomous way.

## SOCIO-CULTURAL DEVELOPMENT

As mentioned above, conditions in society are not just economic but also non-economic, including political, social, cultural as well as defence and security conditions. In GBHN of 1983, Chapter IV, General Pattern of Pelita IV, under the sub-heading Religion and Belief in the Only God, Society and Culture, there are listed ten objectives: Religion and Belief in God, Education, Culture, Science, Technology and Research, Health, Population and Family Planning, Housing and Settlement, Social Welfare, Youth, and Woman Role in Development.



In the pre-condition period for the take-off where we make efforts to strengthen the basic framework, fields which constitute sub-fields of Religion and Belief in God, Society and Culture, must absolutely be developed and increasingly stabilized, in parallel with the development achieved thus far in the economic field. But in principle the development of the socio-cultural field will always relate to spiritual aspects, values system, feeling and intelligence of man. In this regard the key apparently lies in the field of education. Through education we develop the social cultural life of the people as part of the framework we are building and strengthening, and at the same time we prepare the climate and condition for the next period when we have taken off.

The effects of development are certainly not always positive because the so-called side effects will always take place. In religious life, for instance, often arises doubt that as a result of changes which take place in parallel with the course of the development process one tends to be materialistic and go further away from the teachings of religion. What actually happens may not be as bad as assumed, but it is probably true that one becomes ever more critical, realistic and rational, so that his living the belief he adheres to is affected. In other words, changes brought about by development efforts do not only affect the physical world but also exerts influence on the spiritual world involving the living of values and mental attitude.

In GBHN there is among others a provision that religious life and belief in God must be fostered so that a harmonious life can be developed among religious people, among adherents of belief in God, and between all religious people and all adherents of the belief in God with a view to strengthening the unity of the nation and to intensifying good deeds in order to jointly build society. Nevertheless, in the practical social life there are often tensions and vulnerabilities due to differences of religion and belief in God.

One of the aspects of social life which also constitutes an obstacle and sometimes arises as social tension and even social upheavals is the problem of integrating citizens of foreign descent, especially of Chinese descent, into the society of the Indonesian nation. In this regard the General Pattern of Repelita IV which constitutes Chapter IV of the GBHN clearly states: National integration efforts must be promoted in all aspects of life both in the economic and socio-cultural field with the aim of strengthening the unity of the nation and of consolidating national resilience. Here also we are facing realities which are often far from expectation. In spite of the fact that in the past, when the colonial power was prevalent in our country, national fighters and pioneers of independence, already realized that there were indeed disintegrative factors within the body of our nation and society which would divide us when we are not carefull and make no preventive efforts. There are more than one hundred

tribes, each speaking its local language and with customs and ways of social intercourse which differ from each other, which have different religions and beliefs and many other differences. We are also facing the fact that due to the process of our history, there are citizens of foreign descent, both with western and eastern blood.

National unity which must absolutely be supported, cultivated and developed, is certainly not only concerned with the problem of integrating citizens of indigenous and foreign stock, but this process must be carried out as efforts to shape one Indonesian nation, though there are various elements which must be respected as long as they do not endanger the unity of the nation.

It is proper that we are grateful to our fighters of the past, our pioneers and thinkers who have prepared our national independence, who have been inspired by the spirit of burning patriotism and their dedication to the ideals of struggle, have succeeded in establishing the ideal foundation for building the unity of the nation. The third principle of Pancasila which is formulated as Indonesian Unity (and not Indonesian Nationality as proposed by Ir. Soekarno or Nationalism as proposed by Muh. Yamin), and the establishment of *Bhinneka Tunggal Ika* (Diverse but One) as the motto of the state, is clearly no mere chance, but constitutes the result of thinking, reflection and exchange of views which is profound and looking far ahead.

It is likely the task of the present and coming generation to continuously develop and implement that value in real life. We can differ with each other in many things such as religion and belief, tribe, customs, political views, profession, social economic level, descent and the likes, but we also remain one.

Such analysis can be continued and prolonged with regard to other social problems, but one thing is sufficiently clear, namely that our social, socio-political and socio-economic life still contains various vulnerable points which shows in principle that Pancasila values are not yet fully implemented as it should. In the current era of development, these socio-cultural aspects which are directly tied to our values system may become worse when we forget the essential goal of development itself which is of socio-cultural nature as said above.

The President rightly said in his state address of 16 August 1983 that in the period of strengthening the basis during the Pelita IV and V "an overall Pancasila atmosphere" must be created. How such an atmosphere can be created or realized must have the attention and concern of all sides, both state institutions and the government and the whole society. In this connection we return



to the concept of culture of which one of the forms is a complex of values which can only be acquired after a process of learning because they are not rooted in instinct. From this can be drawn the conclusion that education constitutes a very strategic field because it is the key which opens the way in the process of its implementation.

This is the greatest challenge faced by our world of education during the Pelita IV and subsequent periods. Education must be able to be the main support of efforts to strengthen the basic framework, and at the same time to prepare the sound climate for maintaining and developing the further growth rate after we have reached the take-off stage at the end of this century. On the other hand, we are aware that the field of education still contains many weaknesses both in terms of means, system and management, which constitute restraints in facing existing challenges. The situation is sometimes made more difficult due to an inclination toward experimental actions, in addition to statism in attitude or view, generating policies which reduce the room for manoeuvre and complicate all those involved in education. This is certainly not in accordance with the provision of GBHN as the expression of the will of the people, which states on private education: "Private education needs to be upgraded in its quality, role and responsibility in implementing national education and increasingly developed on the basis of the stable national educational patterns, while paying attention to the specific characteristics of those concerned."

We are grateful that in the first year of Pelita IV the field of education is allocated the biggest budget which can be regarded as the expression of a political will to look after and develop the educational field so as to enable it to become a very important supporting element in strengthening the basic framework. Although it should be noted that the large amount of budget is not the only guarantee for success. The right utilization of that budget will very much determine the outcome desired.

Another thing which provides good prospects is the implementation of compulsory education during Pelita IV, in the sense that children of the age group of 7-12 years will be enabled to enjoy primary education, a further step toward the goal of educating the nation. It must be acknowledged that we have achieved some progress in the field of education during three Repelitas, though there are still many unsolved problems. During the period of Pelita IV and subsequent periods our educational system is expected and even required to play a bigger role so as to become the main support of efforts to strengthen the framework, and simultaneously to prepare the new generation to face the future when we have taken off and to continue toward achieving national ideals.

In his introduction in the *Ilmu dan Budaya* (Science and Culture) magazine, Professor Sutan Takdir Alisyahbana has written among other things: "... that the most important question of education faced by our nation is to change mentality, change the structure of the cultural values of our nation so that we get a strong motivation and will to make efforts and work in order to acquire science, economic prosperity and technology ...."<sup>8</sup>

As mentioned above, the pre-condition period is one of transition from traditional into modern society. The traditional mental attitude which has so far dominated the attitude and views of society must be changed into a modern mentality which is more rational, objective and realistic, though it continues to be based on fundamental values because it is just there that lies our identity which distinguishes us as a nation from others.

If during Pelita IV and V we succeed in improving the world of our national education so as to enable it to prepare a younger generation which is truly aware of values and always look for them and examine them, it would mean that efforts to strengthen the basis for take-off especially in non-economic fields for a great deal have been made. We are facing a new stage in national development which demands a new mentality in accordance with that development.

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<sup>8</sup>*Ilmu dan Budaya*, vol. vi, no. 4 (January 1984), p. 242.



# Prospects of Indonesia's Oil and Gas Sector

M.A. WARGA DALEM

## INTRODUCTION

The history of the oil and gas industry in Indonesia is still being written, although it will be 100 years old in 1985. It has been a dynamic history, especially those periods covering the last 20 years. These periods will form the basis for this paper.

The theme -- "Economic Development and Challenges" -- cannot be discussed in any meaningful way without raising the subject of energy. Indonesia enjoys a substantial natural resource in the form of hydrocarbons. Thus, in the development of Indonesia's economy, energy plays a central role as a significant source of foreign exchange and tax revenue. In the last Indonesia's five-year development plan, the Pelita III (1979-1984), the income from oil amounted to an average of 76 per cent of all exports. As such, at least in the foreseeable future, a sound and healthy growth in Indonesia's energy sector is essential to full achievement of its development goals and critical to achieving satisfactory and sustained growth in the economy.

Indonesia has made great strides in the development of its oil and gas resources over the last two decades, so that today Indonesia has a vibrant and dynamic oil and gas sector. In the genesis of this development the national oil company's tasks e.g. Pertamina's, have variously been seen as two-fold:

1. To stimulate exploration and production of oil and gas and thereby provide Indonesia with the required foreign exchange to assist in the nation's overall development program;

2. To provide fuel for the domestic market and the rapidly developing local industry.

Although meeting these requirements is the principal responsibility of Pertamina, the objectives could not be fulfilled as successfully without the cooperation and contribution of foreign contractors and service and supply companies, and the valuable efforts of Indonesia owned and managed companies and Indonesian entrepreneurs.

In order to expedite the development of the hydrocarbon resources, Indonesia began to work with foreign contractors to help provide the country with additional risk capital, advanced technology and highly skilled management. From the perspective of the Korean or Indonesian relationship, one example of this partnership is admirably shown by the Korean Development Company and its joint-venture exploration activity with Pertamina in the North East Java Sea, off West Madura Island.

The means of this cooperation is through the Production Sharing Contract, a unique concept devised by Indonesia in 1966 as a basis for developing its oil and gas resources. The production sharing concept has been adopted, with only minor variations, in many other nations, a fact which attests to its success in accomplishing the purposes for which it was created.

## DEVELOPMENT OF THE PRODUCTION SHARING CONTRACTS

Until 1960, oil and gas concession law in Indonesia had its basis in the East Indies Mining Law of 1899. It is true that, with independence in 1945, the country's first constitution was ratified, and that Article 33 of the constitution is widely interpreted to have superseded the mining law and existing concession arrangements.

It was not until 1951 that a state commission was formed, to draft a new mining law. After many years of deliberation, the commission issued its report. This led to a division of the mining sector into two categories and the adoption of Law No. 44 of 1960, specifically covering oil and natural gas. By operation of this law, the traditional concessionary regime was replaced by a system in which petroleum operations were to be undertaken only by the State and "exclusively carried out" by State Enterprises. This concept derived from the 1945 Constitution prescribed State control of important branches of production affecting the lives of the nation's people, including the exploitation of land, water "and the natural riches contained therein."

The transformation to a production sharing arrangement was not im-



mediate. The earlier concessionaries resisted implementation of the new law and after considerable discussion were able to negotiate "contracts of work" to replace their concessions. Although they were legally relegated to the role of contractors to the State, the change was one of emphasis rather than substance. The foreign contractors were largely able to retain their concessionary prerogatives of management and control over their operations.

The cause of much of the conflict was removed with the founding of "Pertamina" as a single integrated national oil company, and shortly thereafter Pertamina began to utilize the production sharing contract as the vehicle for its management of the exploration and exploitation activities of foreign petroleum companies.

To elucidate, Indonesia's "Production Sharing Contract" has the following major characteristics:

- The management of the operations under the contract is in the hands of Pertamina, and the Contractor is responsible for carrying out the operations;
- The Contractor provides the necessary funds and technical assistance required, and assumes the pre-production risk. Oil production is shared 85:15 after tax. The terms for gas production are similar except that the net to the Contractor is 30 per cent or 35 per cent depending on the time the production sharing contract was signed;
- The Contractor may freely lift its portion of oil or gas and retain its sales proceeds abroad;
- Non-capital costs including exploration and intangible drilling costs may be expensed, and capital costs are depreciated over a reasonable period by the double declining balance method. Interest on loans to finance capital investment, when needed, may be recovered as operating costs subject to Pertamina's approval;
- The Contractor is obligated to supply 25 per cent of its respective crude entitlement to meet domestic market requirements for which the Contractor is reimbursed 20 cent per barrel;
- The contract allows a 10-year maximum for exploration and a 30-year total term if commercial production is established;
- One time agreed signature and production bonus payments are required, as well as mandatory relinquishments of part of the acreage after certain periods of time;
- Title to equipment and data obtained belong to Pertamina, but the Contractor may freely use them for the operations.

In 1977, terms and conditions of production sharing contracts were further improved by introducing an incentive package for new oil fields such that:

- The domestic "prorata" oil is priced at full export value for the first five (5) calendar years of production of each new field;
- An investment credit amounting to 20 per cent of the capital investment for oil production facilities when developing a new field, is allowed to the Contractor before deduction of tax. This incentive is also allowed to full scale secondary recovery projects;
- All capital investments for new oil fields may be depreciated over seven (7) years by double declining balance method; gas fields are depreciated over fourteen (14) years.

Also in 1977 Pertamina entered its first joint venture, or joint operation contract, like that with the Korean Development Company. Under this contract form, companies agree to match Pertamina's previous expenditures in the area or pay all expenses for the first three years, whichever is greater. After that, all exploration and development costs are split 50/50.

In summary, a vital factor in the profitability of oil and gas operations in Indonesia is the favourable nature of petroleum legislation and fiscal condition coupled with an informed and experienced official control. This position has been well accepted by the international energy community, as indicated by the founding of numerous successful partnerships in recent years.

Although 1983 showed a slow-down in contract awards, this was clearly not indicative of reduced expectations on the part of industry nor a lesser attractiveness of the acreage offered, but principally a basic change in circumstances and conditions governing the world energy market. One aspect of this change, has been a significant increase in oil and gas companies acquiring reserves through company mergers rather than through exploration efforts. This moment in history, however, holds no portent for the future.

## FUTURE OUTLOOK OF INDONESIA'S OIL AND GAS

It is true Indonesia is a mature oil and gas producing country with some of the most prolific hydrocarbon production in Southeast Asia. However, Indonesia also continues to be one of the best prospective areas for future oil and gas discoveries and operations.

Indonesia has about 56 prospective geologic provinces which are distributed from the west to the east. Eleven of these sedimentary basins are under



production but most of the basins have neither been drilled nor properly mapped, especially those basins in deep offshore waters.

Basinal areas offshore West Sumatra, off South Java, off the eastern part of Sulawesi, in the Banda Sea and Arafura Sea area and off the northern part of Irian Jaya are the places where extensive exploration has not been fully carried out. Thus, one can honestly say that Indonesia is still in the early stages of exploration and there is plenty of room for growth in its programs. The key is an extensive exploration campaign in the subject regions supported by high exploration technology and heavy capital investment. The risks, apparent in any oil and gas venture, are mitigated by a significant reward opportunity.

Defining new acreages and opening them for generating new contracts is, of course, importing in maintaining and hopefully increasing exploration activity. To capitalize on Indonesia's highly prospective acreage and to draw the oil and gas industry into these so-called "frontier areas," Pertamina has recently instituted a new procedure for open acreage evaluation called the "Technical Evaluation Assistance" contract or TEA. Under this scheme industry can nominate any open area for evaluation, purchase the existing technical data in the area, and if the evaluation is positive submit a bid for a production sharing contract within six months. In the very near future this scheme will also be extended to cover acreage presently being operated by Pertamina.

To supplement this new effort, Pertamina and the Government remain ever vigilant for ways of encouraging higher levels of E & P activity. Certain considerations which must be accommodated include:

- the physical environment in which operations will be conducted; for example deep water or other virgin areas;
- the economics and constraints of developing marginal oil and gas fields, and
- the complementary use of facilities by operators for optimum resource development.

As a result of Indonesia's significant hydrocarbon resources, its forward looking energy planning, and its proven system of cooperation, Indonesia, today, has the capacity to produce up to 1.8 million barrels of oil per day. Out of this total some 1.3 million barrels could be made available for export. Current oil production, however, has been curtailed to 1.3 million barrels per day, excluding condensate, consistent with production quotas established under OPEC guidelines and consistent with Indonesia's support for OPEC's goal to moderate a volatile energy market environment.

In its endeavour to seek out new market opportunities, Indonesia has also

developed a substantial export business in natural gas. In 1983 exports of LNG to Japan amounted to over 9.8 million metric tons or approximately equivalent to 400,000 barrels of oil per day. Most recently, in the expansion of the LNG trade, Indonesia and Korea entered into a significant new trading relationship for 2.0 million tons per year to stream by the end of 1986. The signing of this sales agreement was truly a culmination of concerted efforts built on understanding, cooperation and trust.

So what of the future? Given today's state of affairs, the future of the Indonesian petroleum industry appears unlimited over the next several decades with Indonesia remaining as a major supplier of energy to the world market. Furthermore, oil and gas will continue to play a very important role in the development of our country: as an important source of foreign income, as a major source of energy, and as a provider of new opportunities for employment. The bottom line is that in the fulfillment of national objectives, Indonesia plans to maintain its crude export capability at a minimum of one million barrels per day, and will continue to develop natural gas export as another promising and viable alternative.

To support this level of export, and to meet domestic demand requirements, will be required a constant level of wild-cat and appraisal activity, with new field production off-setting natural rates of decline in older fields.

As discussed before, Indonesia's fiscal environment and prospectivity for additional oil and gas reserves is extremely favourable; thus, the forecast for a similar level of activity, as has been experienced in the past during a period of stagnating world economic conditions and capital constraints, should be viewed as conservative at best.

For each year of the Pelita IV (1984-1989) the objective calls for 67.5 thousand kilometers of seismic and 250 exploration wells. To demonstrate the relativity of this latter number, if you lay a map of Indonesia over a map of the United States, Indonesia would stretch from San Francisco to New York, with about 500 miles to spare. But in 1983, there were only 246 exploration wells drilled in Indonesia compared to about 14,550 in the United States. All things being equal the numbers certainly indicate the early stage of Indonesia's petroleum exploration and the reasonableness of the assumptions for future activity and growth.

By meeting the targets for exploration activity, coupled with a return to a normalized world energy supply/demand balance, Indonesia plans to increase its production from 1.4 million barrels per day currently, which includes 100,000 barrels of condensate, to almost 1.8 million barrels per day by the end of fiscal 1988. It should be noted, in addition to new oil development, that the



utilization of enhanced oil technology will also play a major role in establishing incremental production volumes. This application is particularly important in its ability to stretch out the economic life of our resources.

In the framework of maximizing crude oil exports, during the Pclita IV, Indonesia will continue the development and utilization of other energy resources both as a substitute for oil used in the domestic sector and as an additional foreign exchange earner.

Natural Gas exploration and development has in recent years become an important part of the petroleum industry's growth. Thanks to the very substantial increase in LNG exports there has been a coincident increase in the amount of gas being used constructively.

Within the international LNG market Indonesia's share of the gas export trade has grown significantly since the economic and technical feasibility and commercial potential was recognized over ten years ago. In addition to the recent expansions at both the Arun and Badak LNG plants supplying a new trade to Japanese buyers, a further expansion at the Arun plant will be committed to the new Korean LNG trade. Natural gas production for liquefaction is projected to increase from 2,672 MMCFD under present supply arrangements to 2,952 MMCFD by end of fiscal year 1986.

The role of natural gas in the domestic market is also receiving great attention, and while its use for re-injection purposes for improved recovery in oil producing fields is currently the largest factor in domestic consumption, we envision much greater utilization by domestic fertilizer, steel and cement industries as well as for other industrial and household applications.

Including both domestic and export requirements, it is a current belief that natural gas utilization will increase from the present consumption level of 4,454 to 4,922 MMCF/D by 1988. Under these assumptions flared gas will maintain its current ratio accounting for some 10 per cent of total production. Indonesia is, of course, working hard to find additional opportunities in and around areas where gas is still being flared.

With a view towards new LNG projects, aggressive gas exploration is continuing. Additional gas reserves continue to be discovered in various parts of the country, especially around the existing LNG plants. With this activity, coupled with the large proven gas finds in the Natuna area of the South China Sea, one would expect a continued expansion of our LNG trade. Further, provided markets can be developed, studies continue to be undertaken which would provide the means to substantially increase our LPG production capability.

On the domestic side, one can also mention one other important area of Pertamina's involvement; this concerns geothermal energy. To further ease competitive domestic pressure for crude oil and supplement the use of fossil energy, Indonesia is aggressively exploiting Indonesia's significant geothermal potential which has been variously estimated at some 10,000 MW of energy scattered throughout the archipelago.

To date, however, development plans have been concentrated within the island of Java where Pertamina, in cooperation with the government of New Zealand, operates a 30 MW power station. Additionally, Union Oil in an agreement with Pertamina has also begun to develop geothermal resources in Gunung Salak, in West Java.

Furthermore, Indonesia also plans to greatly expand the production capacity of this resource. In addition to further seismic activity amounting to 350 km<sup>2</sup> per year, its program calls for 20 exploration wells per year, with follow-up development drilling on proven acreage increasing from 25 wells per year currently to some 60 wells in the forward years. The result of this program will allow power generating steam capacity to increase from the equivalent of 30 MW to 390 MW by the end of fiscal 1988.

It is appropriate to mention that Indonesia has also embarked on a much broader diversification of its energy base through the development of coal, hydro and nuclear power, solar energy, wind power and the production of fuel from agricultural products and waste. Exploration and production activities are certainly the mainstay of the development goals; however, Indonesia has also moved to increase the efficiency in its processing sector.

With the exception of the Cilacap refinery, Indonesia refineries were not, in the past, set up to provide the product mix needed internally. Further, due primarily to the age of the refineries, the utilities were energy inefficient. To alleviate this situation expansions were undertaken to add 360,000 barrels per day of effective refining capacity. These new plants are particularly suited to Indonesia's unique domestic requirements, incorporating either a hydro-cracker, as in the case of Dumai and Balikpapan, or a vis-breaker, as in the case of Cilacap. The refinery additions will result in improved yields of needed products, reduced residual production and provide a higher level of product self-sufficiency.

Again in reference to Indonesia's LNG export trade, as the world's largest LND producer, facilities at the Arun and Badak plants will be capable of producing 17.5 million tons of LNG per year from ten (10) trains, when at plateau capacity in 1987. Further development of this resource is planned and proven gas reserves are available provided markets can be successfully developed.



LPG plants at Rantau, Mundu, Arjuna and Tanjung Santan currently have a capacity of 640,000 tons per year. Again, as in the case of LNG, expansion of LPG capacity can be easily achieved dependent on market demand.

Petrochemical plants will also be developed for improved utilization of domestic hydrocarbon resources. A methanol project in Bunyu, East Kalimantan, with a capacity of 330,000 tons per year will produce chemical methanol for utilization as a raw material for the production of plywood glue, solvent, pharmaceutical purposes and export. Additionally, the Aromatic Center project in Plaju, South Sumatra, will produce raw material for the domestic textile industry i.e. synthetic fibers and nylon. The first phase of the Aromatic Center, due to stream in 1986, will be a paraxylene to terephthalic acid unit with a capacity of 150,000 tons per year.

## CONCLUSION

As an overview, this is the direction Indonesia is heading in its petroleum sector. Of paramount importance for this gathering are two clearly discernable factors:

1. Significant hydrocarbon resources and products are available for utilization both internationally and domestically, and
2. Significant opportunity exists for future oil and gas development and the development of the numerous associated up-stream industries.

One aspect paramount to the success of Indonesia's petroleum sector has been the trading relationships it has developed, particularly with Japan where imports of Indonesian crude and LNG account for about 15 per cent and 50 per cent, respectively, of total demand.

The commercial and business challenges to develop this trade have been great, but needless to say it has been demonstrated that these challenges can be met and successfully overcome, which is a tribute to partners in both Japan and Indonesia. This spirit of mutual trust, understanding and dependence has succeeded in integrating a diversity of interests and establishing a working arrangement whereby common interests are profitably pursued and differences settled bilaterally. The underlying factor is the awareness for regional cooperation as a consequence of economic development and economic linkage.

With the signing of Indonesia's LNG sales contract with Korea, Indonesia has entered into a new era of relationship built on interdependence. The signing of this agreement marks more than just the beginning of a new industrial project. This is an event which underscores the strength and confidence in the long term relationship between these two great nations. With this agreement one will succeed in taking one more step towards fostering better mutual understanding between these countries. Inspired by this mutual understanding, it will be easier to reinforce the bonds of friendship and to promote cooperation for future growth.

In closing it is hoped that this paper has given an insight into the many ways Indonesia and Korea could help each other in the development of their respective economies. Large new deposits of hydrocarbon are still there, in Indonesia. Furthermore, in view of the plans and projects mentioned previously, one can witness, in the years to come, all the simultaneous petroleum activities in the country in exploration, exploitation, development of alternative energy sources and expansion of its processing facilities. It is for the business community, the investors and those who have the technology to make use of these opportunities for the sake of common progress.



# **The Conduct of Indonesia's Foreign Policy Over the Next Five Years**

A.R. SUTOPO

At a time when public debates on the various aspects of Indonesia's Pelita IV (Fourth Five-Year Development Plan) occur almost daily public attention to its foreign policy is at the lowest. Within Indonesia's society at large there seems to be an impression -- right or wrong -- that foreign relations do not occupy such an important role as domestic politics. In one way or another, foreign policy is considered a routine task which is the sole responsibility of the government. Such an impression is strengthened by the lack of publications on the various aspects of Indonesia's foreign policy by our bureaucrats or scholars. It seems as if there are no important questions to be discussed regarding the conduct of our foreign policy in the years ahead. In point of fact, the GBHN (Broad Outlines of State Policy) of 1983-1988 treats foreign policy as one of its important fields.

However, as to the conduct of our foreign policy, the current GBHN also provides -- as did the previous ones -- basic guidelines for our executives over the next five years. One of the principles laid down in the GBHN explicitly stipulates that "the conduct of an active and free foreign policy shall consistently be executed to serve national interests, particularly those of national development in all fields." Moreover, it points out the role and arenas in which Indonesia should pursue its goals and ideals outside its national jurisdiction; the priorities to be taken into consideration with a view to those purposes; and the fields of international endeavours in which Indonesia should involve itself, namely international institutions and regional organizations as well as various international forums. In other words, the guidelines incorporated in the GBHN cover virtually all aspects of Indonesia's foreign relations, bilateral as well as multilateral.

It appears that in facing such a wide range of issues, the general public has not been given enough information on the operational aspect of Indonesia's foreign relations. Obviously the GBHN constitutes and provides guidelines for the public should they wish to understand the operational basis of Indonesia's foreign relations. This essay inevitably is largely based on the GBHN. However, the discussion is confined to some aspects that directly affects the conduct of Indonesia's foreign policy over the next five years. Not included is the question on how the formulation of the policy should be done and who is in charge.

To start with, it would be helpful to deal with the basic principles on which the conduct of Indonesia's foreign relations is based. Fundamental to Indonesia's foreign policy is that it is "independent and active" and how Indonesia defines its national interests. Understanding the meaning of those terms would be helpful to understand the priorities established regarding the conduct of Indonesia's foreign policy over a certain period of time in the future.

## THE NATURE OF INDONESIA'S FOREIGN POLICY

Basically, Indonesia's foreign policy is the implementation of the principles and purposes laid down by the Preamble of the 1945 Constitution, particularly the paragraph stating: "... a Government of the State of Indonesia which shall protect the whole of the Indonesian people and the entire homeland of Indonesia and in order to promote common welfare, to enlighten the life of the nation, and to participate in achieving world order based on independence, lasting peace and social justice ..." However, these principles and purposes are the constitutional basis and abstract ideals rather than the operational basis on which Indonesia should conduct its relations with other countries. The GBHN, on the other hand, tries to elaborate those principles and to frame the conduct of Indonesia's foreign policy by adding the adjectives of "independent and active" and reaffirming its purpose of serving its "national interests." These two terms are too often used in public by those who are directly or indirectly involved in the conduct of Indonesia's external relations, but their meaning is not often explained.

With regard to the principles and notion of an "independent and active" foreign policy, it should be noted that it is not a new invention in the record of Indonesia's foreign relations. The very first statement of the principle of an "independent and active" foreign policy was made at a time when Indonesia had to defend its independence. In a speech delivered before the Working Group of the KNIP or Central National Committee (the Provisional Parliament) of Indonesia, titled "Mendayung Antara Dua Karang" (Rowing



between Two Rocks), on September 2, 1948, Prime Minister Mohammad Hatta stated among other things:

"But do we the Indonesian people, struggling for the independence of our nation and country have only to choose to be either pro-Russia or pro-America? Is there no other position we must take in the pursuit of our national ideals?

The Government is of the opinion that the position we must take is that we should not become an object in the international political struggle, but we should go on being a subject entitled to decide our own position, entitled to pursue our own goals ..."<sup>1</sup>

He stated further:

"Indeed, every one of us has sympathy for this or that group, but the struggle of our nation cannot be fragmented merely because of the sympathy, but it should be based on realities, on the interests of our country at any moment ...

However weak we are as a nation who is newly independent compared to the two great powers in confrontation, the United States of America and the Soviet Union, in the opinion of the government we must continue to base our struggle on the adagium: to rely on ourselves and to struggle with our own power and ability."<sup>2</sup>

Thus Hatta explained the position of his cabinet with regard to current international politics. This explanation was also meant as an answer to pressures by the People's Democratic Front (FDR) that Indonesia should openly take sides with the Soviet Union against imperialism. The KNIP then decided to accept Hatta's statement as the guideline for the conduct of Indonesia's foreign policy.

Hatta's statement mentions the existence of constraints in Indonesia's foreign policy, namely the United States bloc and the Soviet bloc; to deal with such an environment, Indonesia should not merely become an object but should be a subject (meaning active) which has the right to choose its own policies and to pursue its own objectives (meaning the principle of independence). Operationally, however, such a principle is determined by "realities and the interests of the country" at any given time. With regard to the option to align with the United States or the Soviet Union and their respective allies, the choice is to be independent in choosing its own way outside "this or that" way. Such a policy does not merely imply neutrality. As Prime Minister Wilopo explained in May 1952, in the conduct of his foreign policy dealing with the two competing and antagonistic blocs, the Indonesian Government has decided to take an independent position, that is: (a) not to take sides permanently by pledging itself to either of the contending parties:

<sup>1</sup>Mohammad Hatta, *Mendayung Antara Dua Karang* (Jakarta: Bulan Bintang, 1976), pp. 117-118.

<sup>2</sup>*Ibid.*, pp. 18-20.

and (b) not to be permanently indifferent or neutral on every issue that may arise from the conflict between the two blocs.<sup>3</sup> But it is frequently wrongly understood that the notion of Indonesia's independent and active foreign policy is identical with that of a neutral position, equidistance, balance in its relations with other countries, particularly in the context of superpower rivalry.

Under the New Order government, basically Indonesia's foreign policy is not different from that laid down by Hatta and Wilopo. The decree of the MPRS (Provisional People's Consultative Assembly) No. XII/MPRS/1966 reaffirmed the basis of the conduct of Indonesia's foreign policy. It is a decree that corrects the defections made by Indonesia during the period of the Old Order regime. It restates the nature of Indonesia's independent and active foreign policy, that is, to serve national interests. That statement is also repeated in the GBHN issued by the MPR (People's Consultative Assembly) in the New Order era, i.e. the decrees No. IV/MPR/1973; No. IV/MPR/1978; and No. II/MPR/1983.

## INDONESIA'S NATIONAL INTERESTS

Here follows a short exposition of the meaning of "national interests" in the context of Indonesia's foreign policy. It is a common place that nations involved in external relations always justify their actions or policies by invoking "national interests." Apparently the use of such a terminology will continue as long as nation-states constitute the basic political unit binding the loyalty of a number of people in the world. In such a situation, statesmen, politicians, diplomats and those who act on behalf of the state will use and place "national interests" above other interests, international as well as sub-national.

Be that as it may, one must acknowledge that within any national society there are interests which may concern only a small part of the people, some groups, a large number of people or all layers of society.<sup>4</sup> Moreover, those interests can be concrete and material goods, but they can also be ideal non-material goods. Whatever kind of interests a state pursues in its relations with other countries will determine the allocation of resources in order to attain or

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<sup>3</sup>Quoted from Mohammad Hatta, *Portrait of a Patriot* (The Hague: Mouton Publishers, 1972), p. 55.

<sup>4</sup>On the concept of "national interests" there are a number of studies and analyses, both on its essence and criticism against its use in international relations. See for instance, Hans J. Morgenthau, *Dilemmas of Politics* (Chicago: University of Chicago Press, 1958); Robert E. Osgood, *Ideals and Self-interests in America's Foreign Relations* (Chicago: University of Chicago Press, 1953); Joseph Frankel, *National Interest* (London: Pall Mall, 1970); and Fred A. Sondermann, "The Concept of the National Interests," *Orbis* (Spring, 1977), pp. 121-138.



preserve those interests in accordance with the realities it is facing. Consequently, the problem is how to put those "national interests" into an order of priorities, since each interest or objective has its own degree of significance.

It is not an exception if that also applies to Indonesia in its efforts to attain its interests and objectives. Indeed, there are interests and objectives that concern the whole nation-state, such as its very existence, but there are also interests that only concern certain groups or a very limited number of people, such as going abroad for the sake of education or sightseeing. There are concrete objectives, such as the improvement of the nation's prosperity and welfare, the establishment of armed forces capable of protecting the homeland and nation, and there are also ideal non-material purposes, such as the democratization of international relations, human rights, and lasting peace in the world. This means that Indonesia needs an order of priorities in the pursuit of its goals and objectives beyond its national boundaries.

## PRIORITIES OF INDONESIA'S FOREIGN POLICY

This essay confines to the environment Indonesia will be facing in the conduct of its foreign policy under the GBHN of 1983-1988. However, in order to understand the priorities of Indonesia's foreign policy, we should first deal with the main underlying policies adopted by the New Order Government. Discussed below are main points taken from the decrees of the MPRS as far as Indonesia's foreign relations are concerned.

The decree of the MPRS No. XII/MPRS/1966 is one of the documents that defines the goals of Indonesia's independent and active foreign policy. It is stated that the goals of such a foreign policy is "to defend Indonesia's independence against imperialism and colonialism in all their forms and manifestations and to uphold the three aspects of the purpose of Indonesia's Revolution, namely: (1) the establishment of the Republic of Indonesia as a democratic Unitary State and National State; (2) the establishment of a just and prosperous society materially and spiritually within the Unitary State of the Republic of Indonesia; and (3) the establishment of good and friendly relations between the Republic of Indonesia and all countries in the world, particularly African and Asian countries, based on cooperation to establish a New World free from imperialism and colonialism directed toward a perfect world peace." In other words, those goals imply efforts to maintain the integrity and unity of the state, to achieve the welfare of the people, and to live in peaceful co-existence and to be good neighbours with other countries. But this decree (No. XII/MPRS/1966) has been revoked by the decree of the MPR No. V/MPR/1973, Article 2, Paragraph 1, because it is already incorporated in the GBHN (Decree No. IV/MPR/1973).

It is stated in the GBHN of 1973-1978 that the conduct of an independent and active foreign policy is to serve national interests, particularly those of economic development, and emphasizes Indonesia's relations with Southeast Asian and Southwest Pacific countries with a view to creating regional stability that will help those countries to manage their own affairs through the development of their national resilience. In this order of priorities ASEAN (Association of Southeast Asian Nations) occupies the most important position. Next are Indonesia's relations with countries and organizations outside the regions of Southeast Asia and Southwest Pacific. The GBHN of 1978-1983 also emphasizes that the conduct of the independent and active foreign policy is to serve national interests, particularly overall development interests. There are no fundamental differences in priorities with the GBHN of 1973-1978.

Apart from those points, the GBHN of 1978-1983 also states the intention of Indonesia to increase its role in the international world in order to foster and strengthen beneficial friendships and cooperation between nations. In this regard, the GBHN of 1983-1988 also points out the need on the part of Indonesia to participate actively in international arenas with a view to establishing a world order with due regard to the limits of its power. In spite of such an intention, the emphasis of the GBHN of 1978-1988 has not changed substantially. As to the field of international relations it is stated in the GBHN that:

- a. The conduct of the independent and active foreign policy shall be carried out consistently and shall serve national interests, particularly overall national development.
- b. Indonesia's efforts and role to participate in establishing a world order based on independence, lasting peace and social justice, through international forums and cooperation, regionally and bilaterally, shall be strengthened in accordance with its national capability.
- c. In that context, Indonesia's efforts and role to participate in solving world problems that threaten peace and are in conflict with the sense of justice and humanity shall be continued and increased.
- d. Cooperation among the countries of Southeast Asia and Southwest Pacific shall be intensified. Particularly cooperation among the ASEAN member countries shall be developed and expanded with a view to strengthening the national resilience of each member country and that of the region towards the creation of a Southeast Asian region which is peaceful, free, neutral and prosperous.
- e. In the context of ASEAN cooperation, cooperative relationships in the economic, social and cultural fields need to be strengthened, both between governments and peoples.



- f. Indonesia's role in the international world in cultivating and strengthening friendship and cooperation for mutual benefit of the nations needs to be expanded and stepped up. Indonesia's struggle in the international world with regard to issues of national interests, such as endeavours to consolidate the implementation of *Wawasan Nusantara* (Archipelagic Principle), efforts to expand Indonesia's export markets, and so on, needs to be intensified as well.
- g. In the context of the struggle for a world order based on independence, lasting peace and social justice, endeavours to establish and strengthen solidarity, common stance and cooperation between developing countries, utilizing forums such as the Organization of Non-Aligned Nations, the Organization of Islamic Conference, the United Nations and others, need to be intensified.
- h. Particularly with a view to establishing a New World Economic Order steps need to be continued, in cooperation with other developing countries, to speed up the achievement of international agreements on commodities, to remove the obstruction and restrictions imposed by industrialized countries on exports from developing countries, and to increase economic and technical cooperation among developing nations, in addition to other endeavours.
- i. Every development and possible world upheavals, both political and economic, should be followed carefully so that possibilities that can affect national stability and obstruct national development can be discovered on time, so that appropriate steps can be taken to secure them. On the other hand, world developments that provide opportunities to speed up the implementation of development need to be exploited for the sake of national interests.

Those main points embodied in the GBHN constitute the direction to be taken by Indonesia. Because this basis clearly shows the existence of linkages between internal affairs and objectives beyond its national jurisdiction, obviously not all of them can be pursued with the same urgency without considering the existing capability to achieve them. Basically this shows that the fundamental norm of an independent and active foreign policy that serves national interests is inspired by the dynamics of the objectives to be achieved in accordance with the existing capability. Due to that dynamics, it wishes to face the ever changing challenges in relations between nations. This is actually the meaning given by the GBHN for the conduct of Indonesia's foreign policy: to act in accordance with realities both within and without national jurisdiction in order to obtain maximal benefits for the nation and state as a whole and to some extent also for the interests of other nations.

## IMPORTANT DETERMINING FACTORS

In the first quarter of 1983, Foreign Minister Mochtar Kusumaatmadja announced that one of objectives of Indonesia's independent and active foreign policy over the next five years is to improve Indonesia's image in the Third World.<sup>5</sup> On the other hand, in his address at the installation of ambassadors to Bangladesh, Iran and other countries in South America on April 13, 1983 President Soeharto said among other things: "... we are also aware that the conduct of an independent and active foreign policy is not easy, particularly in the current world situation."<sup>6</sup> These two statements reflect the dilemma faced today by Indonesia's foreign policy.

Obviously the conduct of Indonesia's foreign relations during the last 15 years has emphasized endeavours to sustain economic development. But Indonesia's economic growth could not merely rely on domestic resources. For that reason it is stated in the MPR's Decree No. XII/MPRS/1966 that Indonesia does not conduct an isolationist nor a neutral foreign policy. If the government has decided to carry out development with the emphasis on the economic aspect, its effect in the conduct of foreign policy is to adopt policies that support those purposes. Since development requires capital goods and domestic resources cannot meet that requirement, the only alternative is to conduct foreign policy with a view to acquiring capital goods and investments from abroad.

In the past such an orientation in Indonesia's foreign policy was obvious, as shown by Indonesia's close relations with capitalist countries -- mostly western countries and Japan. In the view of critics such a policy causes Indonesia to tilt to the West and depend -- to some extent -- on the donor countries and investors. Seen from a different angle, however, such a policy has been chosen by Indonesia itself in order to overcome the difficulties it is facing, taking into account the risks involved in that choice.<sup>7</sup>

Next to this is the top priority given by Indonesia to the region of Southeast Asia in its foreign policy. Indonesia's regional politics during the New Order is

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<sup>5</sup>As to this statement see among others "Politik Luar Negeri RI Tidak Lagi 'Low Profile'," *Kompas*, 22 March 1983.

<sup>6</sup>"Amanat Presiden Soeharto pada Pelantikan Duta Besar Luar Biasa dan Berkuasa-Penuh Republik Indonesia pada tanggal 13 April 1983 di Istana Negara," *Pewarta Departemen Luar Negeri* (April-June 1983), p. 13.

<sup>7</sup>For a thorough discussion on the dilemma of foreign relations between the need to get foreign aid and the problem of dependence, see among others Franklin B. Weinstein, *Indonesian Foreign Policy and the Dilemma of Dependence from Soekarno to Suharto* (Ithaca: Cornell University Press, 1976).



in fact not a new course for Indonesia's foreign policy officials. What is new is the focus of attention on the stability and security of the region that is conducive to economic development. A region of conflicts and tensions, be they caused by internal strife, conflict between neighbouring countries, or interventions by external powers in regional or domestic affairs, is not acceptable to Indonesia because it will disrupt its national interests. In other words, the emphasis of Indonesia's foreign policy on regional affairs is basically security politics and its economic aspect is initially not prevalent. Because of such a decision, the question is not whether that choice is correct but how to make Southeast Asia a region as projected. The initial move taken by Indonesia was to end its policy of "confrontation" with Malaysia and together with other countries in the region to establish ASEAN.

Among various circles, domestic as well as international, ASEAN's achievement has been viewed quite successful. The success of ASEAN is primarily due, according to some views, to its ability to create a political and security atmosphere conducive to cooperation in various fields at the regional level.<sup>8</sup> In the political field for example, inter-governmental consultations among the member countries of ASEAN on intra-ASEAN problems as well as on various aspects of international questions have been prominent. In the security field, ASEAN member countries have agreed to solve their problems by peaceful means. In the economic field, ASEAN has made some success in coordinating their members' policies in dealing with economic powers outside the region, and within ASEAN many agreements on regional economic cooperation have been concluded. However, the region of Southeast Asia as a whole has not developed fully as yet into a truly secure and stable region. Tensions, conflicts, and divergencies still disturb the region. Thus, if Indonesia's regional policies in Southeast Asia do not only concern ASEAN, Southeast Asia as a whole needs to be given attention for the purpose of establishing stability and security in the region.

Three sources of conflict and tension among the countries of Southeast Asia must be taken into consideration. Firstly, there are problems relating to the nation building of each of the countries which is basically domestic in nature, including questions of the state ideology, the distribution of power within the national community, questions of ethnic and religious minorities, separatism and irredentism, and the question of national strategy of development. These problems create not only domestic conflicts and tensions but also, in many cases, some problems in intra-regional politics and relations. Secondly, there is historical antagonism among Southeast Asian countries, such as

<sup>8</sup>The thesis on the political and security aspects of ASEAN has been advanced among others by J. Soedjati Djiwandono, "The Political and Security Aspects of ASEAN: Its Principal Achievements," *The Indonesian Quarterly*, vol. xi, no. 3 (July 1983), pp. 19-26.

political rivalries, historical conflicts, and great differences in culture and identity. The third problem that may lead to conflict and confrontation between countries in the region is the fact that boundaries between them have not been well-demarcated since the post colonial period. Nowadays this problem is more acute in the mainland of Southeast Asia. In the region of the South China Sea, territorial disputes are increasing due to the possibility of finding resources in the area. Among those three problems, historical antagonism and international boundaries are the main sources of instability.

## ACTUAL PROBLEMS

One of the main disrupting factors of the stability and security of South-east Asia is the Kampuchean problem. Seminars have been held and essays written on this problem, while the United Nations and the ASEAN member countries have tried to solve the Kampuchean problem. But so far Vietnam has not made any significant change in its position on Kampuchea. It seems that any solution of this problem has to consider Vietnam's political and security interests in Kampuchea since the Vietnamese intervention in the country is not without legitimate reason. If the proposals of the United Nations and ASEAN to solve the problem have not achieved any significant progress, it does not follow that Indonesia should stop at the ASEAN level in the efforts to solve the problem. There is still a bilateral door open, i.e. direct Indonesia-Vietnam consultations and negotiations, that can be exploited for that purpose and particularly to breach the stalemate. Should the Kampuchean problem remain unresolved, regional stability could be more disrupted if the problem drags external powers into the region's security and political affairs.

The next region of priority is the Pacific area that is simultaneously a complex and promising region.<sup>9</sup> In the Pacific region one can find almost all aspects of international relations. There are developed and developing countries, communist and non-communist countries, Eastern Western and non-aligned countries, capitalist and socialist countries, and the North versus the South. Meanwhile, the Pacific region is regarded as the region with the most dynamic development in the last decade. Moreover, two of Indonesia's main trade partners are located in the area, namely Japan and the United States. And today there are initiatives to establish a forum for economic cooperation in the Pacific region.<sup>10</sup>

<sup>9</sup>Mentioned in the GBHN is the Southwestern Pacific Region. Without ignoring the importance of countries of Southwest Pacific, such as Australia, PNG, New Zealand, and so on, this essay emphasizes the Pacific Region as a whole.

<sup>10</sup>On endeavours toward economic cooperation in the Pacific Region and its problems, see among others Hadi Soesastro and Han Sung-joo (eds.), *Pacific Economic Cooperation: The Next Phase* (Jakarta: Centre for Strategic and International Studies, 1983).



There are four major powers actively involved in the politics, security and economy of this region, namely the United States, the Soviet Union, the PRC and Japan. At first there was a view that in the Pacific region a tripartite relationship would develop between the United States, the PRC and Japan, to counter what was regarded as the expansionism and the increasing hegemony of the Soviet Union. Actually relations between the United States and the PRC face constraints and obstacles, such as the United States position on Taiwan and its relations with ASEAN countries, with the result that those relations cannot develop to become an Sino-American alliance. China itself that has been struggling for her four modernizations (those of the economy, industry, defence, science and technology) is still showing an uncertain direction in the future like many other developing countries.

However, one needs to take into account that the Sino-Soviet rivalry and conflict and the tripartite rapprochement between the United States, the PRC and Japan has resulted in an increased deployment of the military power of the Soviet Union in the Pacific region and the Far East. In this regard, one thing that must be taken into account is the increasing power and presence of the Soviet Navy in the Asia-Pacific region, particularly in connection with the use of the Cam Ranh and Da Nang base facilities in Vietnam. Although there are efforts of rapprochement between China and the Soviet Union, the latter seems determined to maintain and increase its military presence and facilities in the Pacific region. The reason is that the Soviet Union, like other major powers in the Asia-Pacific, desires to become a big power in this region. In addition, the Soviet Union has political and military commitments in this region that must be maintained, just like other major powers. Therefore it is no exaggeration to say that the Pacific region is regarded to have quite strong linkages with the national interests of countries which regard themselves as part of this region. Indonesia is one of those Pacific countries.

Because of those politico-strategic and economic considerations, Indonesia's dependence on countries in the Pacific region and on the security and stability of the region becomes real. Given the interdependence between Indonesia and other countries in the Pacific area, it is not wise to ignore developments in the political, security and economic fields or to react a priori to them. Isolating itself from the course of developments in that region is not the best response for domestic development because Indonesia's political, security and economic interests are partially tied to this region. Since the problem concerns many parties, accommodations to existing realities are needed. How is Indonesia's involvement in the region considered the most dynamic in the world? How to response to political and military developments in the region, particularly as far as it concerns the PRC's and the Soviet Union's involvement? What kind of politics are needed to face industrialized countries

and the new industrializing ones in this region for the benefit of national development, particularly with regard to Indonesia's export-import balance?

The desire to improve Indonesia's image in the international world implies in principle complex policies on various important problems, not only in the Southeast Asian region but also in other regions of the world. Those policies are like a two-edged knife: on the one hand, they must determine a political position on various basic issues that are faced by various regions of the world, and hence have consequences in bilateral relations; on the other hand, they must support an economic strategy (particularly one that is linked to export objectives) which has the most direct impact on economic policies. For that reason bilateral relations will always be important for those goals. Maintaining and expanding existing relations, for instance, with countries which up to now have been good partners and friends in political as well as in economic terms, constitutes one of its tasks. Another step is to develop those policies with other countries that so far have got little attention, such as the Third World or socialist countries.

When the offensive of those policies cannot be launched against all countries, then the case in point is to determine the priority of region or country that is considered to have the potential for those goals and can be reached with the existing capability. This is important particularly as far as Indonesia's bilateral relations are related to policies in various international forums and organizations, such as the Non-Alignment Movement, the Islamic Conference Organization and the United Nations. Efforts to achieve and further a united stand and cooperation among Third World countries need not be opposed to efforts to expand export markets to developing countries. Or the struggle to establish the New World Economic Order does not mean creating constraints to the strategy of developing export markets. To that end firmness of policy and speed to act by executives responsible in the political as well as in the economic fields is needed. It follows that domestic coordination constitutes an unavoidable requirement.

An illustration of that question is Indonesia's view that the Non-Aligned Movement and the Islamic Conference Organization constitute important forums that must be taken into account in international politics, both as a means to seek and preserve international peace and as a vehicle in developing constructive relations among Third World countries.<sup>11</sup> Although these forums are important, it cannot be denied that today they are facing real and fundamental challenges regarding their own identity, unity among their members,

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<sup>11</sup>On these forums, see among others Mochtar Kusumaatmadja, *Politik Luar Negeri Indonesia dan Pelaksanaannya Dewasa Ini* (Bandung: Alumni, 1983), particularly Part II, Chapter 2 and 4.



and the effectiveness of their actions.<sup>12</sup> Although there are slogans with a tone of solidarity and unity among their members, dissensions in their respective forums cannot be hidden, both due to superpower influence that has exerted upon them because of member countries who follow a radical and conservative course, and on account of disputes and conflicts among their respective members. Aware of the fact that such international forums are facing a dilemma, Indonesia's firm stand in the face of various issues among Third World countries need always to be maintained so that the already complex problem in this regard does not lead to a doubtful decision making in Indonesia's foreign politics (and economics). How is, for instance, Indonesia's stand on the Iraq-Iran conflict, on Egypt's position in the Arab-Israeli conflict, and what are the consequences of the endeavours to increase trade relations with the countries mentioned?

Briefly, the conduct of Indonesia's foreign policy today takes place in an era that requires accommodation efforts in customs that have developed in international relations and are linked not only to bilateral relations but also to multilateral ones through various international forums and institutes regarding various problems, such as peaceful co-existence, arrangements on the use of air space, sea area, exploitation of natural and other resources, international trade, protectionism, population, information, human rights, disarmament, and other problems that cannot be listed here one by one. I mean, if Indonesia's image is to be improved in international arenas, institutes dealing with those international issues should show that Indonesia exists among them. The experience in fighting for the Archipelagic Principle may be one of the instances of that ability and perseverance.

## CONCLUSION

Generally, there are two main points in the conduct of Indonesia's foreign policy. Firstly, there is the desire to conduct an independent and active foreign policy with a view to improving Indonesia's image in the international world as one of its tasks. This main point constitutes traditionally a guidance for officials and decision-makers especially as far as the policies of the present government are concerned. Secondly, there is the fact that the injunction to serve national interests is in practice facing limitations. Development endeavours in all fields, with the understanding that economic development constitutes one of the central themes, is still facing limitations to rely on resources available in the country. The requirement of funds, capital goods, technology and even skills needed to manage them cannot be fully met with available domestic resources. Also from the angle of economic interests today

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<sup>12</sup>Compare among others with Fabio Tana, "Hard Times for Third World Bodies," in *Politica Internazionale* (Spring, 1983), pp. 83-92.

the need for a larger and bigger markets for Indonesia's products, both raw materials and industrial goods, is felt increasingly urgent in order to maintain the development momentum already established. On the other hand, the situation and developments in foreign environments are not always favourable to those goals.

In the face of those complexities, the task of Indonesia's foreign policy is to balance things considered essential simultaneously to various international realities. Relations of a bilateral nature, particularly with traditional partners, are still a fundamental part. Due to existing limitations to increase relations, for instance trade and investment, on the part of partners considered traditional, such as Japan, the United States and West European countries, opening new bilateral relations with potential countries in various regions of the world constitutes an increasingly urgent requirement. In turn, initiatives taken by Indonesia to response to its external environment are also increasingly needed. The reason is that a part of Indonesia's national interests is outside its national jurisdiction.

When the burden from external environment becomes bigger and hence requires the conduct of an active foreign policy, establishing a kind of alliance whether formally or not will result in alternative limitations to carry out the mission entrusted. To a certain extent, Indonesia, in its judgement, has succeeded in maintaining the independence of its foreign policy. What is needed today, among other things, is to increase relations with other powers and potential so that its flexibility is maintained and ever growing. Relations with the so-called "new industrializing countries" in various regions of the world, with socialist countries, and with potential regional countries in a more intensive way can be conducive to flexibility in choosing alternatives when traditional partners are showing the maximum limit they can cope with. These bilateral relations will become stronger when "obligations" that are multi-lateral in nature can be met, in relations both with international organizations and multilateral forums.

Given the objectives to be attained and the heavy burdens, the problem partly returns to the interior too. Work coordination between parties connected with the conduct of foreign relations and policies becomes an imperative, particularly in order to avoid bottlenecks that may be caused by the bureaucracy. That coordination is concerned with work in each institute or department and coordination between departments. This implies that real ability is required from departments that are directly or indirectly involved in problems on foreign relations and those on international relations, such as the law of the sea, international development, food, health, disarmament, protectionism, the use of air space, and the like. To that end are required bureaucrats who are adept administratively but also experts who master special fields in international relations.



# Book Review

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## Political Agriculture

***Political Agriculture and Rural Development*** (in Indonesian: *Politik Pertanian dan Pembangunan Pedesaan*) by Mubyarto. Jakarta: Sinar Harapan, 1983, 300 pp. This review article is written by Dr. Djisman S. Simandjuntak, Head of the Department of Economic Affairs, CSIS.

As pointed out by the author in the introductory chapter, this book is intended to be used for a systematic study of political agriculture at the tertiary level. Before going into details, the author clearly puts forward the concept of political agriculture, the similarities and dissimilarities of political agriculture vis-à-vis agricultural policy, and the link between political agriculture and rural development. He explains all this in order to avoid confusion with regard to his discussions and interpretations later in the book.

In Chapter II the author discusses in an elaborate manner the relationship between the peasants and the government within a historical framework, that is, from the pre-colonial period and the post-colonial period to the period of independence. Through this historical study the author tries to show that the behaviour of the peasants today stems from an obvious background in the past. In this framework he points out that the be-

haviour of "as long as it pleases the patron" does not seem to have faded away in Indonesia, and its negative impact has often been felt. The suffering of the Javanese peasants, he says, was due to a discrepancy between theory and practice, especially between agricultural policy and its implementation.

After discussing the relationship between the peasants and the government within the historical framework, the writer presents in Chapter III the basic concept of political agriculture. In this chapter he points out that agriculture has flourished everywhere since time immemorial, even in the absence of government. In this modern age, he says, one cannot imagine any agricultural activity without government interference. Basically, however, one has to understand that agricultural development without agricultural "politics" from the government is not at all impossible. One may even say that the absence of government interference in any agricultural activity may be regarded as one form of political agriculture. The author says, furthermore, that many countries, perhaps including Indonesia also, have to face various problems owing to lack of concrete data for use in the formulation of agricultural policies. Quoting Dr. A.T. Mosher's view, the author mentions the three roles a minister of agriculture is supposed to play -- as administrator, ambassador of agriculture, and agricultural expert.

In analyzing the various aspects of the theory of political agriculture in Chapter IV the author argues that it is not possible to discuss the politics of rural and agricultural development without directly linking it to the national political economy. Political agriculture,

he says, may have to give way to political economy regarded as being wider in scope and significance. Thus in this chapter the theory of political economy and the contribution made by other social sciences like anthropology and sociology are briefly discussed. In this context the author also states that Western economic theories may be adopted in Indonesia but they are inseparable from other social sciences.

In Chapter V the author expounds some concrete cases of the various aspects of agricultural policy with a discussion also of certain commodities such as sugar and a number of export products. By studying the data and samples given one will immediately notice the weaknesses and problems found in the agricultural sector. Apart from this, the author also illustrates the importance of coordination among the government agencies concerned with agriculture.

The author divides his discussion in the next four chapters into two sections of two chapters each. In Chapters VI and VII he confines his deliberation to that part of agricultural policy that deals with agricultural efficiency and ways on how to improve it. This means a discussion of the growth aspect of political agriculture and the programs that stimulate export and increase food production.

One of the most important aspects of political agriculture is the land issue which covers ownership, use, lease and control of agricultural land. It is not a new one and is, in fact, the oldest in Indonesia's history of agricultural economy. By providing data the author points out that the control and ownership of agricultural land leaves much to be desired and has brought about negative excesses in its wake. There is a law which regulates and prevents these excesses from occurring, but the problem lies in its enforcement. This, he points out, is due to feudalistic elements which have not as yet been completely eliminated from Indonesian society. Basically, feudalism is a system of social relationship between lord and vassal, the former determining the life of the latter. In a state where the feudal system prevails laws and regulations are invalidated and replaced by a

relationship that is based on loyalty between lord and vassal. Under this system it is the lord (and the highest is the king) who owns the land and all the vassals under him are merely tenants or more precisely appanage holders.

Land reform has not as yet been successfully carried out in Indonesia. In this context the writer discusses in detail the land reform issue starting from concept, purpose and implementation to the period covering the last few years. As a complement of Chapter VI, he also analyzes issues on irrigation, intensification, agricultural credits, mass guidance, and the future of the intensification program.

Pricing and marketing policy is the theme of Chapter VII. In this chapter the author discusses the policies adopted by the government with regard to agricultural prices, both in terms of output and input. In studying this issue he points out that pricing policy concerning output is inter-related with, or has an impact on, input. He says that although the main objectives of the Bureau of Logistics (more intimately known as Bulog) are: (1) to maintain the minimum rice price; and (2) to stabilize the rice price in order to prevent it from exceeding the maximum level, it appears at first glance that no problems exist because the former deals with incentive to rice growers while the latter is concerned with consumer protection, but in reality these objectives are in conflict with each other. On the other hand, although the role of middleman is not desirable, it is not easy for the farmers to get rid of this link between producers and consumers.

Chapters VIII and IX deal with the aspects of equity in agricultural development. This section is concerned with rural development with special emphasis on the total development of man in the rural area. The discussion on cooperatives in these chapters is interesting. The writer points out that the concept of cooperatives is fourfold, namely: (1) cooperatives as an ideology or movement; (2) cooperatives as part of society's development activity and as a development activity for mutual cooperation; (3) cooperatives as a form of business enterprise; and (4) cooperatives as a



means of implementing the government's economic policy. The author makes this differentiation in an attempt to show the role and position of the cooperatives in Indonesia's national economy that is in accord with the 1945 Constitution and the problems that might be faced.

With regard to transmigration, the writer believes that in order to make it a success the final decision to transmigrate must rest with the people concerned. The gap between expectation and reality may be the cause for the transmigration program to fail in the process, all the more so if the expectation is aroused by the incentive factor that is either invented or exaggerated.

In Chapter X the author tries to reflect on what he has discussed in order to find out whether, viewed from its theoretical perspective, a valuable lesson can be inferred from it. In one of his conclusions he says that the dual nature of Indonesia's agriculture still prevails. It has left its mark on various aspects of agricultural and rural development. Thus whatever policy the government is going to take, it certainly has to take the consequences arising from it into account. Maybe, the writer says, this is the development "theory" that we are looking for, but probably not one but two or more theories that cannot be separated from one another. In this connection, the author points out that agronomists and sociologists in Indonesia's rural areas have hitherto often referred to the involution and dualism theories of Clifford Geertz and Boeke and to the theory of shared poverty. Although these theories have time and again been criticized by Indonesian research workers, it has to be admitted that the Indonesian experts themselves have yet to find their own theories. And this certainly serves as food for reflection!

The dualism theory is applied in Indonesia for the purpose of differentiating the nature of agriculture, both in and outside Java. Many research projects have been conducted and reported, but so far these are mostly concerned with conditions in Java. The fact that the government has not yet adopted a clear-cut policy on rubber and coffee confirms the truth of the criticism that Indonesia's political agri-

culture is still "Java-centred" or insufficiently orientated to the problems faced by the farmers (and the estates) outside Java. This situation should be rectified through the introduction of "reforms" in many of Indonesia's agricultural development policies. It is said that Java should belong to the past, Sumatra to the present, and Kalimantan (with the exception perhaps of East Kalimantan) to the future.

At the conclusion of his book, the author says that the attitude of economists who regard themselves more realistic and empirical does not deserve any praise. They think that the economic theory to which they have adhered is quite adequate and requires no correction when applied in Indonesia.

The book presents on the whole a clear and adequate analysis that is in accord with its theme. The information given in it will enable readers to understand the various agricultural policies and the basic theories or scientific bases that go with such policies. In analyzing agricultural and rural development in Indonesia within the historical framework the author has succeeded in presenting both the successes and failures attendant upon it and the problems which are being faced and have yet to be faced. He has also launched some sharp criticism here and there, but this is important if an optimal result is to be achieved.

Indeed, the data presented by the author are often of a general nature, cover only part of Indonesia, and do not as yet reflect the final condition. However, it can nevertheless be said that to a certain extent the picture given does not diminish the significance of the problems presented.

As mentioned earlier in this review, the book is intended to be used as a text-book for the systematic study of political agriculture at the university level. However, because of the meaningful contribution that it makes, the book is also very useful for policy-makers since it reveals things which will be of great help to them in their efforts to continue with their development programs, especially in the agricultural field.







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